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**ABSTRACT**

This review discusses the fiscal difficulties of the City and School District of Philadelphia and describes the projection of expenditures and receipts and the mounting deficits implied by these projections. Three different projections are made to point out alternative fiscal outlooks: a high projection that corresponds to strong economic conditions and aggressive spending; a medium projection that assumes some strengthening in the economy and slower paced public spending; and a low projection that corresponds to weak recovery and little attempt to increase the amount of services provided by government in Philadelphia. The article summarizes the projections, and emphasizes the medium projection. An appendix includes a more detailed description of all projections. (Author/JF)

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THE FINANCIAL FUTURE OF  
CITY AND SCHOOL  
GOVERNMENT IN  
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BUSINESSES REVIEW

## IN THIS ISSUE

This issue of the *Business Review* reports exclusively on the fiscal difficulties of the City and School District of Philadelphia. It describes projections of expenditures and receipts and the mounting deficits implied by these projections. The outlook is not a promising one. Expenditures may exceed receipts by about a half-of-a-billion dollars by 1975, with smaller but growing deficits in years leading up to 1975. Higher taxes, some budget trimming, and sharply increased aid from Federal and Commonwealth Governments may be required to close the deficit.

Inflation may account for over half the increase in spending between 1970 and 1975. But it will not produce an equivalent increase in revenues. Wages paid by businesses in Philadelphia—the base for the City's wage tax—have grown less rapidly than those paid by government. In addition, the taxable value of real property, which forms the basis for City and School District property taxes, has shown little responsiveness to inflation.

But inflation may not be the only reason for large spending. Very sharp increases in the amount of health and welfare services provided by the City are likely. Moreover, continued expansion in staff of the School District seems probable. When inflation and growth in services are combined, expansion of about 120 per cent in the total budgets of the City and School District seems likely.

The fiscal outlook of the City and School District is far from definite, of course, and several different projections have been made to point out alternative outlooks. Specifically, three projections have been made: a high projection, corresponding to strong economic conditions and aggressive spend-

ing; a medium projection, assuming some strengthening in the economy and slower paced public spending; and a low projection, corresponding to weak recovery and little attempt to increase the amount of services provided by government in Philadelphia. It is the middle projection that produces the deficit of \$5 billion. If the low projection holds, the deficit would be \$.3 billion. And, it would be \$.7 billion according to the high projection.

The article summarizes the projections, and emphasizes particularly the medium estimate. The Appendix includes a more detailed description of all projections.

Staff members of the Fels Institute of State and Local Government, under the direction of Dr. Julius Margolis and Mr. Morton Lustig, carried out most of the work on projection of expenditures. David Lyon of the Federal Reserve Bank carried out the projection of revenues and the final analysis of expenditures with the help of Alice Coblenz, Kathryn Kindl, and Richard Epps. Catherine Defina was principally responsible for editing this report.

The Federal Reserve Bank would like to thank the many people who provided help and advice. Though it is hard to single out any individuals, we would like to offer special thanks to Romanus Buckley, Director of Finance, City of Philadelphia, Richard Gilmore, Deputy Superintendent for Administration, School District of Philadelphia, and their respective staffs who proved invaluable in providing information. Also, we would like to thank Lennox Moak, Director, Pennsylvania Economy League, for his helpful criticism.

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FEDERAL RESERVE BANK OF PHILADELPHIA

## The Financial Future of City and School Government in Philadelphia

by David W. Lyon\*

Philadelphia taxpayers will face red again this Spring—the red ink of impending fiscal deficits for the City and School District of Philadelphia. Certainly they have faced deficits before, but never have the deficits been so large as recently. Causes of this growing fiscal gap are clear. While spending has mushroomed, the local tax base from which the City and School District must draw a large share of their new funds has inched upward slowly.

The taxpayer views this higher government spending as a burden, but sees no out. A large low-income population and dilapidated physical plant have made Philadelphia's role in the war on poverty, slums, and crime especially large. Costs of bearing these expanded responsibilities have been boosted by accelerating inflation in the private sector—and by substantial increments in paychecks of public employees.

So, as spending has intensified, taxpayers

have witnessed a larger chunk of their earnings eaten away by new taxes and increased tax rates. But most of the new taxes have produced less revenue than expected, have been expensive to collect, and one has been rescinded by the courts. More important, new tax structures and rate increases have, at best, filled only one year's deficit.

The crush of new spending has left little time for developing more reliable and longer term solutions. With the hope of providing citizens some insight into the future, we have examined the outlook for expenditures and revenues of the City and School District of Philadelphia. Projections were made of both the growth in government services and the impact of inflation on government costs and revenues. The outlook described by these projections is for greatly

\* With the assistance of Richard W. Epps.

increased fiscal deficits for City and School government in Philadelphia—reaching a half-billion dollars for the year 1975, even if payments from the Commonwealth and Federal governments continue increasing as they have recently.<sup>1</sup> This deficit may be preceded by smaller but growing shortages. Without early fiscal action, the deficits of all the years between now and 1975 could cumulate to over one-and-a-quarter-billion dollars. Higher tax rates, new intergovernmental aid, and some budget cutting are the options that

must be relied upon to close these deficits. Such efforts will be made by local leaders and will alter the projections included here. Thus, the projections are not forecasts of what will occur in future years, but a description of problems that must be faced.

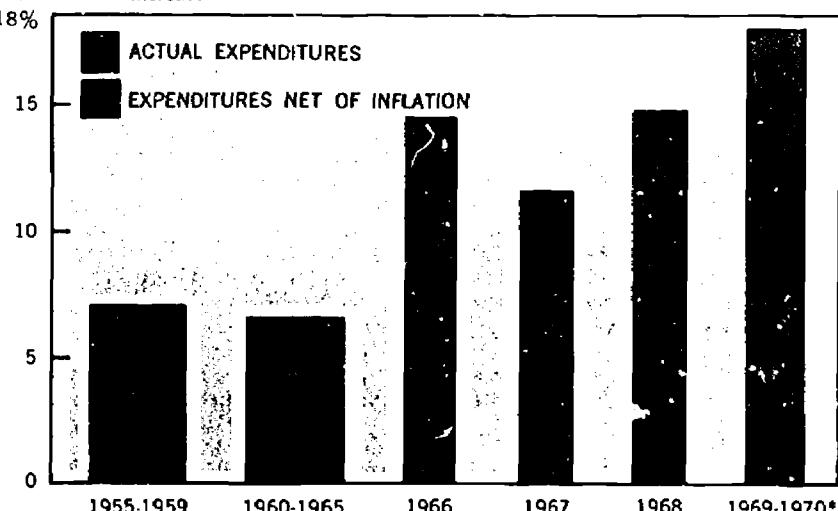
### THE BILLOWING BUDGET

Spending by the City and School District of Philadelphia has shifted into high gear in recent years. As shown in Chart 1, recent yearly increases in combined school and

CHART 1

THE PACE OF GROWTH OF SPENDING BY THE CITY AND SCHOOL DISTRICT OF PHILADELPHIA HAS DOUBLED IN RECENT YEARS. MOSTLY BECAUSE OF INFLATION.

Annual Rate of Increase



\*The years 1955 through 1965 correspond to calendar years for both the City and School District. The years 1966 through 1968 correspond to calendar years for the City and fiscal years for the School District, with 1966 representing fiscal 1967, 1967 representing fiscal 1968, and 1968 representing fiscal 1969. Finally, 1969-70 corresponds to the 1970 fiscal year for both the City and School District. All later years are fiscal years.

<sup>1</sup>The projections are for operating expenditures of the City and School District plus payments for debt service.

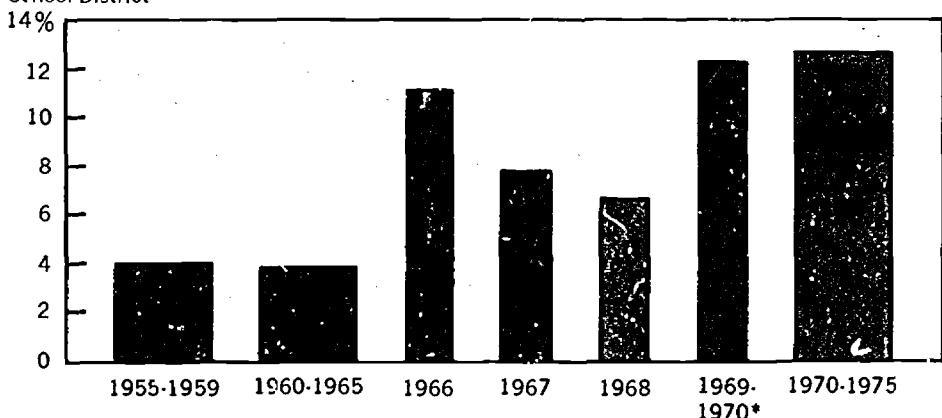
municipal expenditures have doubled over the rate of previous years. Although decisions by local government leaders to expand

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CHART 2

THERE MAY BE LITTLE RELIEF IN INFLATION FOR THE CITY AND SCHOOL DISTRICT DURING THE NEXT FEW YEARS.

Annual Rate of Increase for Wages and Prices Paid by the City and School District



\*See note to Chart 1.

services have added to the public bill, the principal spending thrust has been from inflation.

THE HEAVY HAND OF INFLATION

While present in earlier years, inflation did not become an important problem for Philadelphia government until the late 1960's. (See Chart 2) Small but tolerable increases in governmental costs began to snowball in 1966 as workers in local government here began to demand higher wages. In that year, the average wage paid by the School District jumped 16 per cent and that paid by the City climbed 10 per cent. In the next two years, wage gains subsided a little, and then jumped by 12 per cent in 1969. Justifiable or not, these increases were far above the rate of expansion of wages in the rest of the economy.

While labor is the largest item on local government's shopping list, the City and

School District also purchase materials and services. These nonlabor items, which compose about a third of the local government budget, have shown less-marked price increases than has labor. However, their prices began to escalate at ever-greater rates near the end of the 1960's as local and national economies heated up.

As inflationary pressures ease, expansion in costs of the materials and services will slow. But this relief may not find its way to the labor bill, at least not in the near term. Government workers in other large cities have set an example of greater militancy with "job actions" and outright strikes. If these actions spread to Philadelphia, a quick softening of wage gains seems unlikely. Should this be the case, inflation in wages and materials would raise prices paid by Philadelphia government by 60 per cent from the 1970 fiscal year to the 1975 fiscal year. This inflation is only a little less than that of recent years.

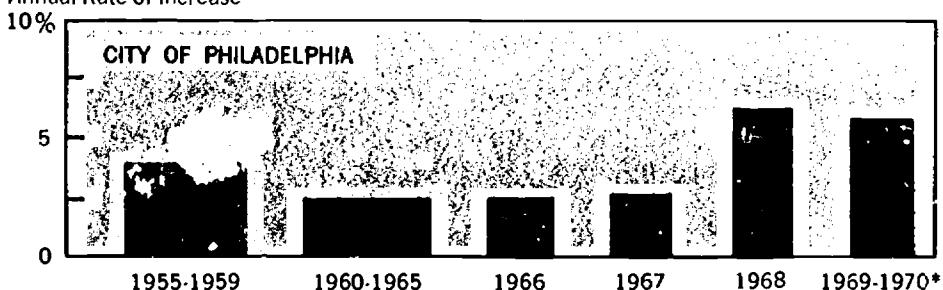
### EXPANSION OF SERVICES

Inflation, which has had a staggering impact on the local public budget, is not the sole source of fiscal pressure. As shown in Chart 3, real expenditures (net of inflation) of the City and particularly of the School District increased during the late sixties, reflecting improvement and expansion in public services.

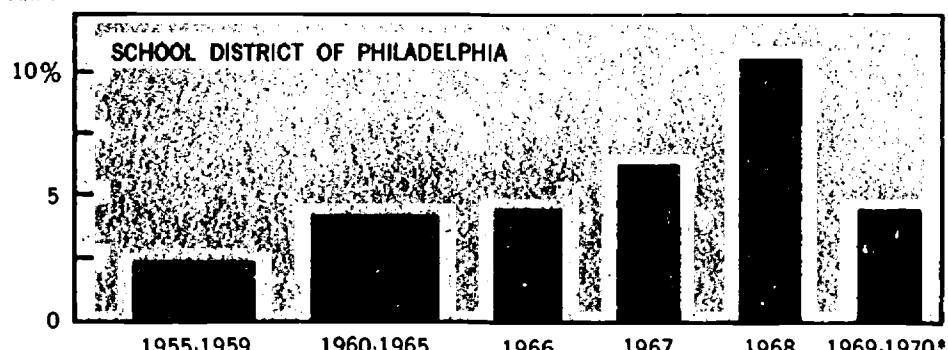
#### CHART 3

EVEN ABSTRACTING FROM INFLATION THERE HAS BEEN RAPID, ALTHOUGH IRREGULAR, GROWTH IN (REAL) EXPENDITURES.

Annual Rate of Increase



Annual Rate of Increase

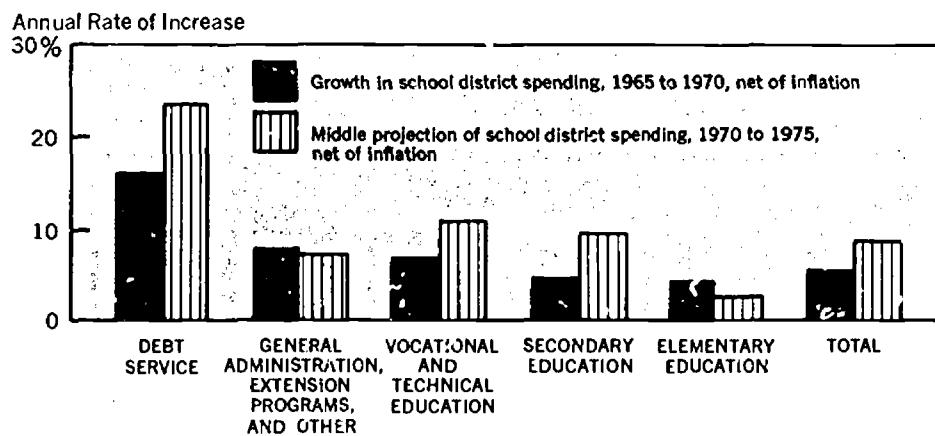


\*See note to Chart 1.

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**CHART 4**

ASIDE FROM INFLATION, OUTLAYS FOR DEBT SERVICE, GENERAL ADMINISTRATION, AND EXTENSION PROGRAMS HAVE SPEARHEADED THE GROWTH IN SCHOOL SPENDING. ALTHOUGH ADMINISTRATIVE AND EXTENSION COSTS WILL SLOW IN THE FUTURE, THE SLACK WILL BE MORE THAN TAKEN UP BY COSTS OF SECONDARY AND VOCATIONAL-TECHNICAL EDUCATION.



\*The lighter bars correspond to our medium projection. Lower and higher projections are presented in the appendix.

Philadelphia schools is still severely behind national averages in basic skills, such as reading.

Commendable efforts to bring performance of Philadelphia schools in line with expectations have been made in recent years—but they have cost money. Special schools for pre-school children, specialized teachers for basic skills, teachers' aids, and enlarged and modernized school buildings all have been added to the system in recent years. These improvements and some new ones will probably be extended in the future. But the full character of urban education is still unfolding.

Officials of urban schools are experimenting to find the most effective combination of efforts to educate city youth. This process of experimentation makes the future form and cost of the School system particularly uncertain. Our projection for School spending is conservative, since we have assumed little change in the way the School District attempts to educate the young. Drastic new methods of education eventually may lower the cost of running the schools, but will more likely increase the cost, at least in the short run. Thus, our projection of costs, shown in Chart 4, is probably somewhat low and is best interpreted as basic

expenditures to which will be added the cost of any new, trial methods of education.

1. **New Staff.** The principal tool that the School District has used in recent years to improve education has been that of providing more attention to each child. This intensified effort has meant sharp increases in staff of the District. While student enrollment has increased by only 5 per cent, school employment has jumped by one-fourth. Half of the new staff are teachers, and half are nonteaching assistants. More teachers mean smaller classes, and assistants free teachers of clerical and other chores.

What staff increases have meant in terms of improvement in education is not yet clear. While greater educational resources have been expended, the composition of enrollment in city schools also has shifted towards students with different learning problems. Moreover, the search, supported by the expanded staff, for more successful methods of education is a long-term effort.

The most likely expectation for the future is that the recent gradual increase in educational staff will continue. The middle projection, presented in Chart 4, is based on an extension of the staff expansion that occurred in the last four years. Higher and lower projections, included in the Appendix, are based, respectively, on the staff trend of the last two years and last six years.

2. **Enrollment Shift.** Recent increases in total enrollment have been concentrated in elementary grades. But a drop in the birth rate and slowing of in-migration into the city in recent years will ease the pressure on elementary enrollments. As current elementary students work their way to the upper grades, secondary students will become a larger share of total enrollment. Since a larger complement of both teachers and assistants is used in upper grades than in primary grades, more students in secondary schools will spell higher total costs for the schools.

3. **New Schools.** Debt service has been, and will continue to be, the most rapidly growing element in the education budget. Expansion in enrollment has begun to burst the seams of the aged education plant in Philadelphia. Double shifts and temporary classrooms have been necessary. So, the School Board has begun a long-range program of building which stretches out beyond 1975. Thus far, most construction has been of elementary schools, but current efforts are focusing on secondary facilities.

Tight conditions in monetary markets and a ceiling on the rate of interest that the School District can pay in its borrowing combined to slow the building program during 1969 and 1970. However, as monetary conditions ease, the District will attempt to catch up on lost time as well as carry out previously scheduled construction. Easing in interest rates also will lower the cost of money for the District, but expansion in borrowing will more than offset this small gain. And, increases in debt service to support the accelerated building program will be compounded by payments for bonds sold to balance the 1970 operating budget of the School District.

4. **Total School Spending.** According to our middle projection, shown in Chart 4, total expansion in the School budget may be about 50 per cent more rapid in the coming years than recently, not including the effects of inflation. Greater debt service cost and the enrollment shift would cause this more rapid upsurge. Overall staff expansion would continue at the rate established in the last four years, with some emphasis on new personnel to support rising secondary enrollment.

**Municipal Services.** Spending by the City has grown more regularly through the years than has spending by the School District. (See Chart 3.) In large part, this is a reflection of the variety of functions the City performs and the latitude it has to balance its

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spending among them. During the early sixties, for example, when police expenditures were rising rapidly, expenditures for other categories, principally street maintenance, were cut. Recent growth in pension payments may have caused government officials to restrict growth of health, welfare, and capital spending. The School District, in contrast, produces just one product—education—and has less range within which to balance priorities.

Over the long term, the City has had some of the same goals as has the School District—social and economic development of the city, for example. And, these goals will probably affect the composition of future spending by the City, with health, welfare, and

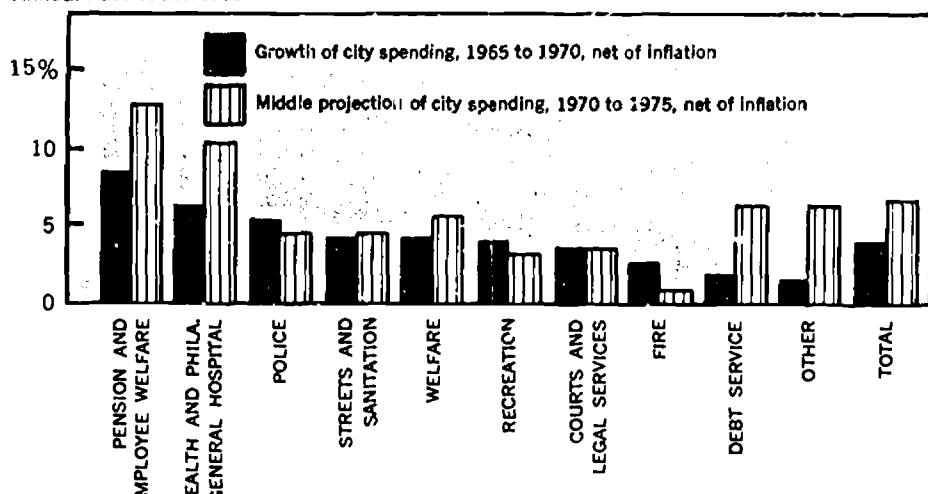
debt service to support construction receiving emphasis. Spending on pensions probably will continue to grow as the required City contribution is escalated by wage increases.

1. Pensions. Three distinct factors have caused a rapid run-up in pension costs. First, during the middle sixties, City contributions to the pension fund were abnormally low, and the previous balance in the pension fund was drawn down to support the monthly checks to beneficiaries. As the City resumed a higher and more adequate level of payment into the pension fund, the expenditure naturally grew. Second, pension benefits were substantially liberalized in the late sixties,

#### CHART 5

ALTHOUGH ALL CITY FUNCTIONS HAVE SHOWN SOME INCREASE, THE HIGHEST RATES HAVE BEEN FOR PENSIONS, HEALTH, AND POLICE. OUR PROJECTIONS ARE THAT FUTURE GROWTH WILL BE COMPARABLE, BUT WITH SOME CHANGES IN EMPHASIS.\*

Annual Rate of Increase



\*The lighter bars correspond to our medium projection. Lower and higher projections are presented in the appendix.

calling for increased contributions by the City. And, finally, the rapid increase in wages paid to City employees took its toll in terms of increased pensions to newly retired workers.

During the early 1970's, the City's rate of contribution to the pension fund will be reevaluated, and probably increased. The City is required to regularly examine the adequacy of its current contribution to the fund, to determine whether the level is sufficient to cover pension liabilities being incurred. The present rate of contribution, determined by an evaluation in 1967, is based upon the assumption of a very low increase in wage rates paid by the City. The next evaluation probably will assume a somewhat higher rate of wage increase and thus lead to a higher rate of contribution by the City. This alteration may cause a growth in pensions for the next few years comparable with that experienced recently.

**2. Health.** Rising expenditures for both health and police reflect fundamental pressures upon the city. Major health outlays support the Philadelphia General Hospital and community health care of various forms. Growth of these outlays reflects intensified efforts to aid the low-income population of the city. Only a part of the motivation for expansion in the health area lies with the City, however. All real growth in health services has been supported by Commonwealth and Federal aid to Philadelphia. As more intergovernmental aid is pumped into the City, and as the low-income population of the City continues to expand, we may expect health care to grow at even more rapid rates than it has up to now.

**3. Police.** Wages are the main reason that the police budget has grown. Also, the size of the police force has expanded steadily in all years except 1966, as a public concern with crime has forced continuing expansion in police services. The steady growth was broken in 1966 as the capacity of the

patrol and administrative staff of the Department jumped. Continued steady expansion is expected in the future.

**4. Other Expenditures.** Most remaining elements in the City budget—streets, welfare, recreation, courts, fire, debt service, and miscellaneous—have grown, and are expected to grow, at moderate rates. We expect, however, rates of growth for expenditures on fire protection, debt service, and the miscellaneous category to change significantly. Real expenditures on fire protection will grow less rapidly in the future, since staff expansion to support only two new fire stations is scheduled during the next five years. On the other hand, costs of debt service will jump dramatically, predominantly to support investment in Philadelphia International Airport. (This increase, however, will be offset by an equal increase in revenues from the airport.) Finally, growth in the miscellaneous category, which has been below its historic levels in recent years, will expand at a rate close to that of total City expenditures.

**5. City Total.** Combining all City categories, we project an annual rate of expansion of 6.5 per cent for the City budget. This is about one-half higher than the 4.0 per cent growth posted in the late sixties. The increased expansion reflects, chiefly, increased debt service and health and welfare services.<sup>2</sup>

#### TOTAL BILL

Including inflation, growth in public services could mean a thumping 120 per cent increase in expenditures for the City and School District combined between 1970 and 1975. (See Chart 6.) The middle current-dollar projection continues the trend established in the late 1960's, with high and low

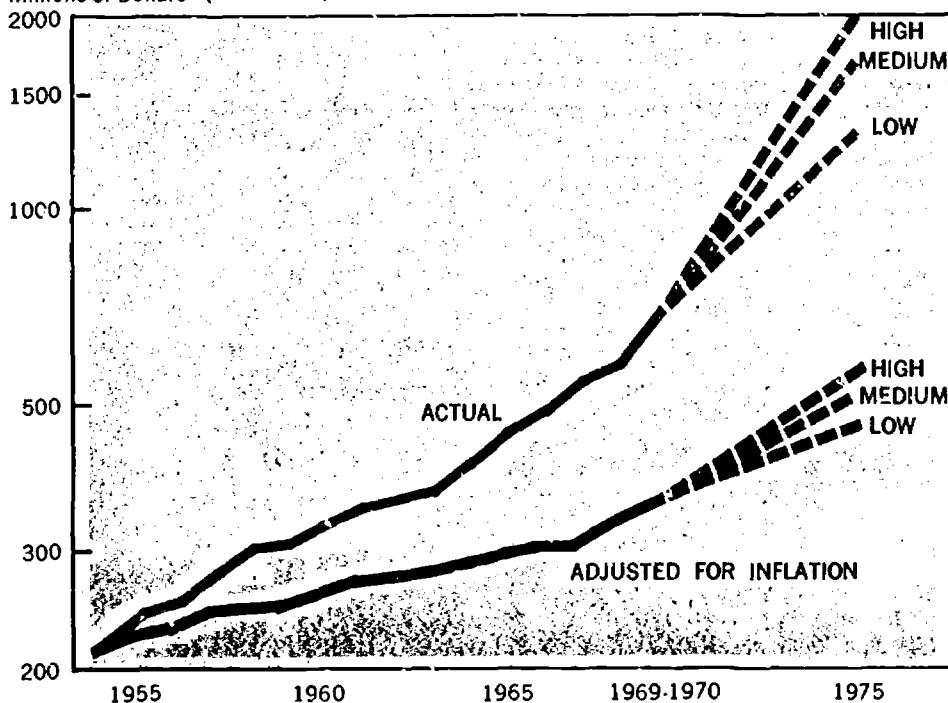
<sup>2</sup>This is our most probable or middle expectation. As explained in the Appendix, a very tight economy may push this rate of growth up by a point, and a weak economy may lower it by a point.

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CHART 6

WHEN PRICE AND REAL GROWTH PROJECTIONS ARE PUT TOGETHER, EXPLOSIVE GROWTH IN CITY AND SCHOOL SPENDING RESULTS.

Millions of Dollars (Ratio Scale)



estimates deviating only slightly from the past trend. The projection includes more real growth and less inflation than in the past few years. Thus, while taxpayers again may have to face a doubling in the public bill, as they did during the late sixties, they may expect the gain in services to make up a larger part of the growth.

### PAYING THE BILL

While public spending in Philadelphia has been on the upsurge, the tax base has not kept pace. Were it not for hefty tax hikes, additional taxes, and massive intergovernmental aid, Philadelphia's public sector now would be hopelessly mired in debt. And the

financial road in the 1970's promises to be even more rocky. The City and School District may face a combined deficit of \$500 million in the fiscal year 1975, even if tax receipts continue a normal growth and nonlocal aid increases sizably. If intergovernmental aid does not grow, the deficit could reach \$700 million.

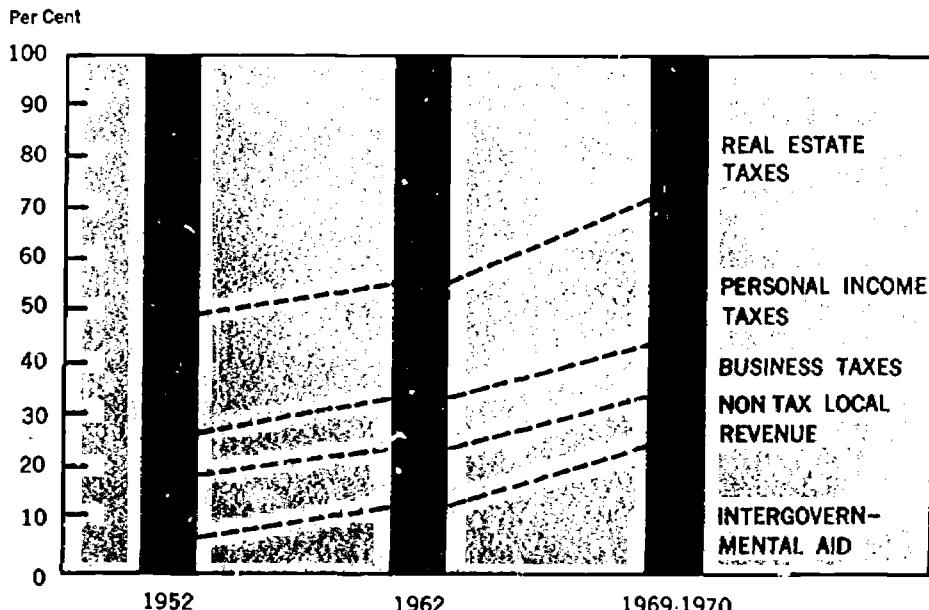
Support for Philadelphia's public spending comes from several different sources—local taxes, Commonwealth aid, Federal aid, and a host of smaller local fees, fines, and service charges. Local sources have been shouldering less of the burden in recent years. As shown in Chart 7, the share supported by

local revenues has dropped from about 93 per cent of total government receipts in Philadelphia to about 77 per cent between 1952 and 1970.

Part of the relative decline was planned. Both states and the Federal Government have gradually accepted the idea that services to the large low-income population in old cities like Philadelphia are a responsibility of more fiscally fortunate taxpayers across the state and nation. Perhaps necessity has been more forceful, however, in lowering the relative share of revenues raised locally. The increasing low-income population and static economy of the city, which have led to increasing

#### CHART 7

**LOCAL TAXES HAVE BECOME A SMALLER PART OF CITY AND SCHOOL DISTRICT REVENUES AS INTERGOVERNMENTAL AID HAS MUSHROOMED AND REAL ESTATE RECEIPTS HAVE LAGGED.**



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demand for public services, have also slowed growth of the local tax base. Local support, therefore, has become more difficult to generate as demands for service have surged.

#### THE LOCAL YOKE

Personal income earned by residents of Philadelphia is the principal source from which local taxes must be paid. This resource base has not grown nearly so fast as has spending for education and municipal services. (See Chart 8.) Still, leaders of the City and School District have tried to keep local tax receipts up with spending. So, they have levied sharp tax hikes which have taken a bigger bite out of Philadelphians' budgets.

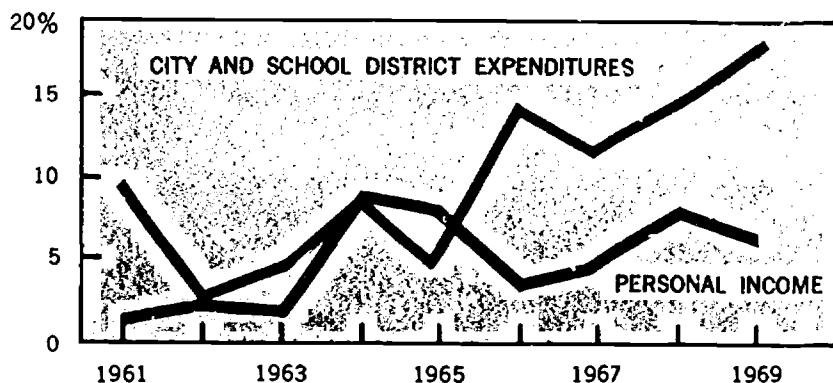
from 6 per cent in the late 1950's.<sup>3</sup> The problem is aggravated further, because the base upon which local taxes are levied—income, real property, and business receipts—has not kept up with growth in personal income. Slow growth in the value of taxable real property is the main cause of this lag.

**1. Real Estate.** While personal income has increased by 43 per cent since 1960, the value of taxable real property has advanced a paltry 15 per cent. Lagging demand, particularly by high- and middle-income families, for housing in the city, low investment in industrial properties, and a significant expansion of tax-exempt properties all contribute to this sluggish growth.

#### CHART 8

#### GROWTH IN CITY AND SCHOOL SPENDING HAS OUTSTRIPPED GAINS IN PERSONAL INCOME OF THE CITY'S TAXPAYERS.

Annual Rate of Increase



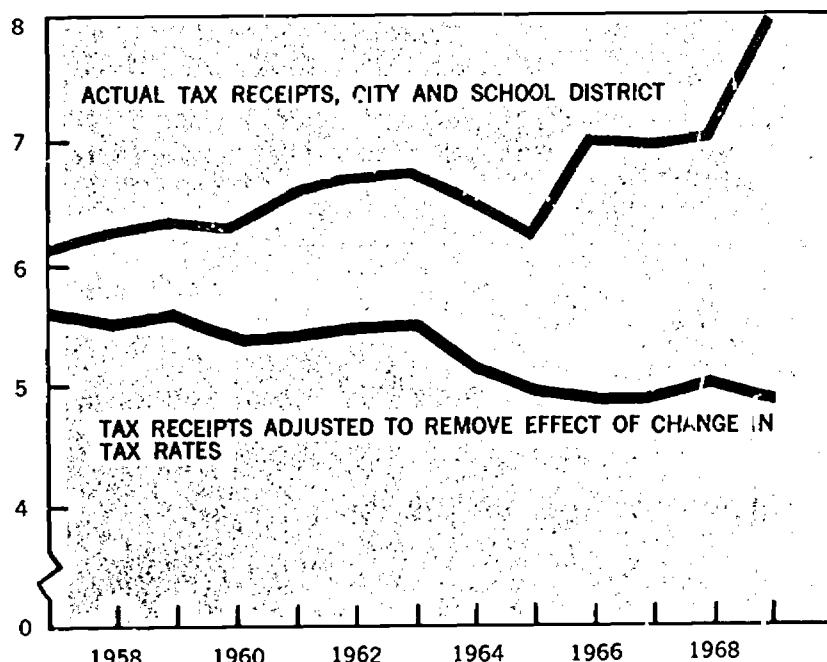
As shown in Chart 9, because of advances in tax rates and creation of new taxes, tax receipts now equal nearly 8 per cent of total income earned by residents of the city—up

<sup>3</sup>This measure of tax burden includes collections from business and industry. However, personal income is closely related to the changing value of production in the city. Comparison of personal tax collections with income yields similar results.

## CHART 9

SLOW GROWTH IN THE TAX BASE OF THE CITY HAS REQUIRED FREQUENT INCREASES IN TAX RATES, AND AN INCREASING BURDEN ON TAXPAYERS.

Per Cent of Personal Income



Because of this lag, the real estate tax has declined in importance as a source of revenue. In 1952, the City and School District relied upon the real property tax for half of their revenues. Today, real estate tax receipts have slipped to only 27 per cent of the combined City and School District revenues (Chart 7).

**2. Real Estate Substitutes.** To relieve pressure on the sagging real property base, the City of Philadelphia has increased its wage

and earnings taxes. From a rate of 1.25 per cent on earned income in 1952, the City gradually jacked up the rate to 3 per cent in 1969—a 140 per cent leap. This increase compares with an expansion of only 39 per cent in the real estate levy from \$1.70 per \$100 of taxable value in 1952 to today's rate of \$2.375.

Intergovernmental aid provided another means of relief. The School District turned to the Commonwealth when spending began to outpace sluggish real estate revenues in

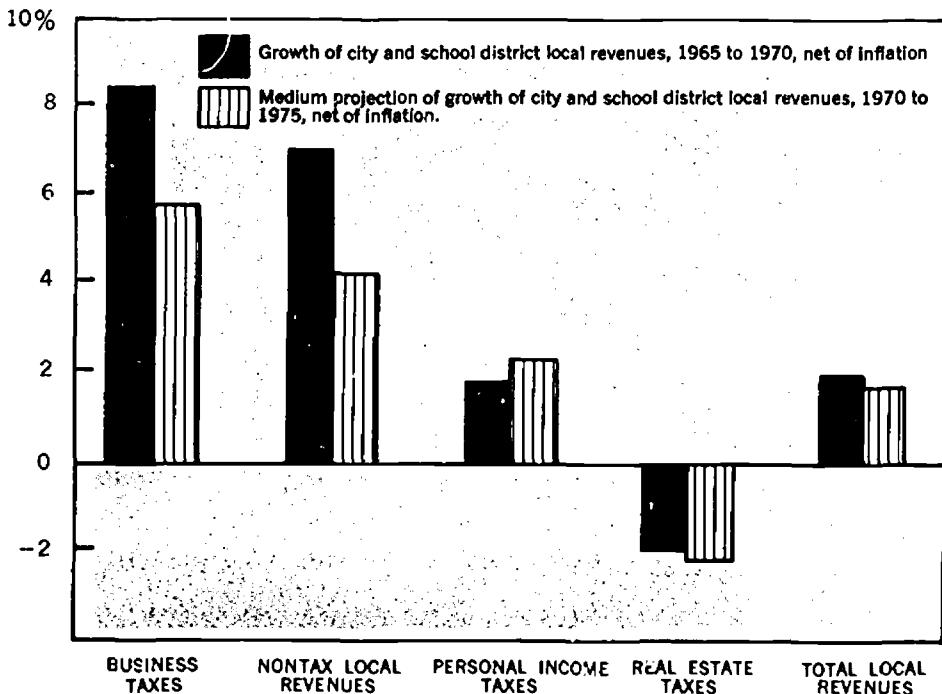
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the early 1960's. Commonwealth aid to the School District jumped from 20 per cent of all revenues in 1952 to just over 50 per cent in fiscal year 1970. During the same period, real estate tax receipts plunged from 65 per cent to 34 per cent of total School revenues.

**3. The Prospects for Local Revenue.** Infla-  
CHART 10

IN THE PAST NEW BUSINESS TAXES AND NON TAX REVENUES PUSHED UP LOCAL RECEIPTS. WITH LESS HELP FROM THOSE SOURCES IN THE FUTURE, TAX RECEIPTS MAY GROW MORE SLOWLY.

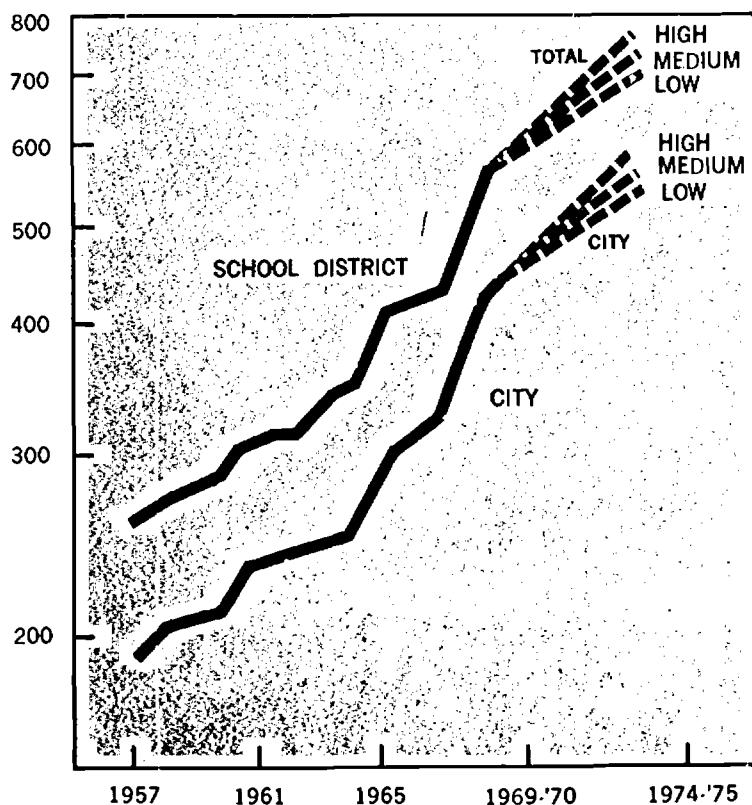
Annual Rate of Increase



\*The lighter bars correspond to our medium projection. Lower and higher projections are presented in the appendix.

**CHART 11**  
**GROWTH OF LOCAL REVENUES WILL SLOW SOME**  
**WITHOUT NEW HIKES IN TAX RATES.**

Millions of Dollars (Ratio Scale)



estate tax, net of inflation, will probably decline, as they have in recent years, because of slow expansion in the assessed value of real property. Business tax revenues probably will shift to a lower course, even with the addition of the School District's new com-

mercial occupancy tax. Business tax receipts jumped sharply in the late 1960's with the addition of the School District's corporate net income tax. The new occupancy tax likely will produce less of a proportionate expansion because the business tax category

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is larger now. Growth in local nontax revenues may taper off as rents from International Airport slow from their recent spurt. Added up, total tax and nontax local revenues probably will continue to have weak growth (net of inflation) into the 1970's—down to a 1.7 per cent annual rate from the 2.0 per cent rate of the late 1960's.

Inflation will raise tax receipts as personal income and business profits respond to higher prices in the economy. Real estate revenues, however, will show little response to changes in the rate of inflation and thus will grow at about the same pace, regardless of economic conditions. Our expectation is that the average rate of inflation in consumer prices may be about 4.5 per cent during the early 1970's. Real growth in tax receipts and inflation, when combined, may push City revenues up to \$670 million in

1975 and School District revenues up to \$460 million. (See Chart 11.)

These tax receipts will not be enough to cover expenditures. Assuming intergovernmental revenues remain at 1970 levels and tax rates are not increased, a combined City-School District deficit of three-quarters-of-a-billion dollars would remain—\$325 million for the School District, and \$400 million for the City. (See Table 1.)

#### INTERGOVERNMENTAL AID

During the '50's and '60's, urban centers in the nation, particularly large central cities, became the homes of millions of low-income families. Lacking adequate skills for long-term employment, most families leaned on the local public sector for education, health, welfare, and recreation services. However, there were severe inequities in the ability of

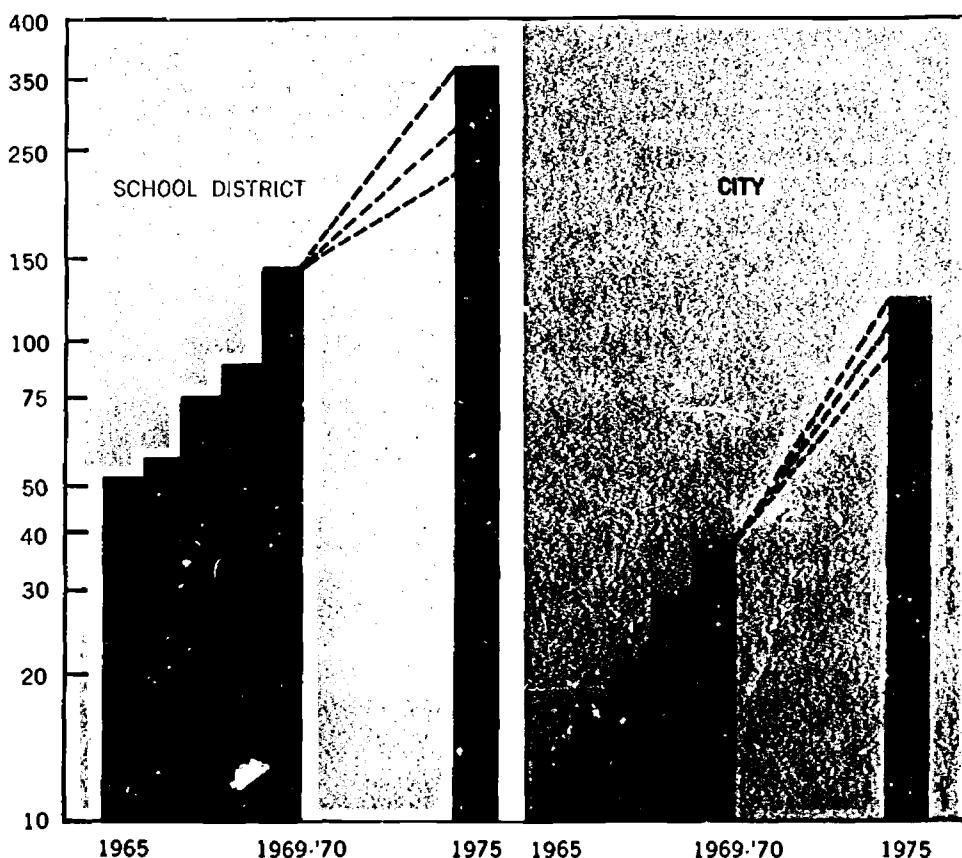
**TABLE 1**  
**A PROJECTED INCOME STATEMENT FOR FISCAL 1975**  
(millions of dollars)

	City			School District			Combined City and School District		
	High	Med.	Low	High	Med.	Low	High	Med.	Low
Expenditures	1,200	1,000	787	747	643	552	1,947	1,643	1,339
Salaries									
Local Revenues and Existing Levels of Intergovernmental Aid	616	594	572	327	319	313	943	913	885
Resulting City deficit									
Intergovernmental Aid	584	406	219	420	324	239	1,004	730	454
New Commonwealth Contribution									
Other Commonwealth Contribution									
Other State Contribution									
Total City deficit	59	72	56	210	142	86	301	214	144
Total City would be	493	334	189	210	182	151	703	516	310

CHART 12

PAYMENTS TO PHILADELPHIA BY THE FEDERAL AND COMMONWEALTH GOVERNMENTS HAVE INCREASED SHARPLY, THOUGH IRREGULARLY. CONTINUATION OF RECENT TRENDS WOULD CAUSE INTERGOVERNMENTAL AID TO MORE THAN DOUBLE BY 1975.

Millions of Dollars (Ratio Scale)



## FEDERAL RESERVE BANK OF PHILADELPHIA

local governments to support essential services, and increasing numbers of municipalities faced erosion of their tax bases. So, it was imperative that Federal and state revenues be used to tackle the job of improving public services.

Most of the intergovernmental aid programs that proliferated during the 1960's emphasized assistance for local services whose benefits may "spillover" into other communities—particularly health, education, and welfare services. Nearly 95 per cent of aid received by Philadelphia in 1970 was for these purposes. Education probably will continue to glean the lion's share of intergovernmental assistance in the 1970's.

**1. To the School District.** Since 1965, intergovernmental revenues to the School District have grown from \$54 to \$146 million—a 160 per cent increase. (See Chart 12.) The bulk of this aid comes from the Commonwealth of Pennsylvania. The future of Commonwealth aid to the School District is fraught with uncertainties. Recent increases in subsidy payments have been erratic and explosive. The Commonwealth upped its subsidy payments by 2 per cent between 1965 and 1966, but in the fiscal year 1970 raised them by nearly 60 per cent. Uncertainty also is compounded by the budget battles that periodically rage in Harrisburg.

Large jumps in aid during the late 1960's resulted, in part, from hard campaigning by leaders of Philadelphia, and also from some special factors, such as the revision in the Commonwealth formula for providing aid. Further large jumps seem improbable. A likely expectation is that aid to Philadelphia schools will grow at about the rate posted for all schools in the Commonwealth. Our projection would place Commonwealth aid to Philadelphia schools at \$280 million in 1975—a 15 per cent annual rate of increase (Chart 12).<sup>4</sup> Of course, all of this assumes the

<sup>4</sup>The high projection, 348 million dollars assumes a 20 per cent annual rate, and the low projection, 226 million dollars assumes a 10 per cent annual rate.

Commonwealth is able to get its fiscal house in order.

**2. To the City.** Intergovernmental aid to the City, while only a fraction of its revenues, has increased sharply—from \$12 to \$38 million between 1965 and 1970 (Chart 12). The largest portion of this aid supports health and welfare services. Even in light of the Commonwealth's fiscal problems, these social services are likely to continue to receive high priority into the 1970's. Consequently, it seems reasonable to assume that the City can anticipate continuation in the recent rate of growth of its intergovernmental receipts—24 per cent annually to a level of \$110 million in 1975. But, of course, problems faced by Commonwealth and Federal governments could make a shambles of this projection.

### IN THE RED

Even if these rather hefty increases in intergovernmental aid materialize, the City and School District would still face a combined deficit of approximately \$520 million in 1975. (See Table 1.)<sup>5</sup> Without action between now and 1975, deficits will pile up each year, cumulating to nearly \$1.4 billion. According to our middle projection, the combined City and School District deficit might look like this:

1971	\$ 60 million
1972	140 million
1973	235 million
1974	370 million
1975	<u>516 million</u>
Cumulative total \$1,321 million	

Of course, these projections assume that intergovernmental aid comes through as it has in the past—a fairly shaky assumption. Even if it should, however, immediate and continuing action on tax increases or economy measures or both will be needed.

<sup>5</sup>This is not a cumulative deficit, but outstanding bills for just the fiscal year 1975.

## PLUGGING THE GAP

Even assuming growth in tax revenues and rapid expansion of nonlocal aid, new measures must be implemented to head off fiscal chaos in the 1970's. One alternative, President Nixon's revenue-sharing proposal, holds promise of easing the burden on local governments. But higher tax rates and some new taxes very likely will have to be added to the existing package of local collections. Also, public pressure will continue to mount for budget cutting.

## NEW DOUGH: REVENUE SHARING

By 1975, Federal revenue sharing could help relieve Philadelphia's financial headaches. The current Presidential proposal would give \$5 billion of "new money" to the states and cities of the nation. Under the proposed formula of distribution, the City would receive \$44 million, and the School District would garner the more modest sum of \$10 million.<sup>1</sup> Of course, passage of the measure is far from assured. And, some of the principal bills that may supplant revenue sharing would provide little direct help to Philadelphia. A Federal take-over of responsibility for supporting monthly welfare payments, for example, would ease the Commonwealth's problems. However, since Philadelphia's welfare responsibility does not extend to financial aid to the needy, the proposal would be of little direct aid to the City.

## UPPING THE LOCAL ANTE

On the local front, pushing up tax levies is often the first tack taken when deficits appear. One strategy for the future would be to jack up rates at a pace similar to recent trends. How much would this strategy produce? A one-point jump in the wage tax to

4 per cent, for example, would account for \$92 million of new revenue; a 5 per cent increase in the real estate tax would yield \$7 million; and a one-point increase in the unincorporated business net profits tax to 4 per cent would produce \$7 million. If revenue-sharing funds were forthcoming and the City of Philadelphia instituted these tax increases, its deficit would still be \$180 million.

For the School District, tax increases would be less fruitful. None of the large taxes which make up its local revenue—the real estate tax and corporate net income tax, for example—keeps up with the economic growth of the city as does the wage tax. Consequently, even substantial increases in tax rates would not generate enough revenue to plug the deficit. Increases consistent with past jumps in the School District's two big taxes would generate only \$30 million in new funds. This amount, combined with \$10 million in revenue-sharing funds, would still leave the School District with an \$140 million deficit in 1975 (Table 2).

**New Nuisances.** Possibly, sharp-eyed officials can find new local sources of funds. The principal sources of revenue—personal income, real property, and business receipts—are already being tapped. Thus, new taxes must be on narrower bases, and collections would be smaller. A further problem with new taxes is that unless they are planned ahead, local officials may be forced, as they have been in the past, to push the measures through with little time allowed for attention to details.

Two recent taxes of the School District illustrate. One, a tax on sale of liquor at bars and restaurants, was declared illegal a few months after enactment, but after the School District had begun to count on it. The other, a tax on payments by business for rented space, is being collected, but the proceeds are expected to be small, and collection costs may be high.

With \$140 million in outstanding bills to be met in 1975, School leaders may be

<sup>1</sup>This estimate derived from *Federal Revenue Sharing with State and Local Governments*, U.S. Department of the Treasury, July 1970.

## FEDERAL RESERVE BANK OF PHILADELPHIA

**TABLE 2**  
**FILLING THE DEFICIT: ILLUSTRATIVE PROSPECTS**

City of Philadelphia (millions of dollars)	Total Deficit in 1975	School Dis- trict of Philadelphia (millions of dollars)
(\$330)	<b>44</b>	(\$180)
	<b>Federal Revenue Sharing</b>	10
	<b>Local Tax Rate Increases</b>	
7	Real Estate Tax—Increase 5 per cent, from \$2.375 to \$2.50 per \$100 assessed value.	Real Estate Tax—Increase 19 per cent, from \$2.10 to \$2.50 per \$100 assessed value.
92	Wage and Earnings Tax—Increase 33 per cent, from 3 per cent to 4 per cent.	Corporate Net Income Tax—Increase 33 per cent, from 3 per cent to 4 per cent.
7	Business Net Profits Tax—Increase 33 per cent, from 3 per cent to 4 per cent.	
(\$180)	<b>Remaining Deficit for Fiscal Year 1975 (middle projection)</b>	(\$140)

tempted to invent four or five new small taxes. An early start on these taxes may help. But the pay-off is bound to be small, expensive, and uncertain.

#### TRIMMING THE FAT

Cost-cutting is the other side of the fiscal coin, and beleaguered taxpayers have been outspoken in their demands for budget cutbacks. Unfortunately, savings from budget trimming may be less lucrative than many critics expect.

Budget trimming may be done in two ways—improving the efficiency of government or cutting the services provided by government. Undoubtedly, some inefficiency is present in Philadelphia schools and government. Inefficiency can be found in almost

all agencies and firms. However, the amount that could practicably be eliminated is probably small and would go only a short way towards plugging the gap.

The other line of budget trimming is by way of reducing the services performed by City and School government. Certainly a large part of the impending deficit could be eliminated in this way. Voters constantly decide on what they want government to provide, and they may cut back their demands as new, higher prices for government services are established. However, the appeal of service-cutting, strong in the abstract, is less appealing when translated into specific cuts like fewer police, less hospital care, or fewer teachers—each of which provides an important service in the eyes of some segment of the community.

## NO PANACEAS

Philadelphia's financial crisis will continue into the 1970's. Spiraling costs of labor, a sagging local tax base, and highly uncertain assistance from other levels of government will complicate the yearly task of balancing the City and School District's budgets.

Several alternatives are available for closing the prospective gap in the public budget—new or higher local taxes, greater aid from the Commonwealth and Federal governments, and reductions in the local public budget. Also, a number of new measures which would directly or indirectly aid the ailing public sector are waiting in the wings: revenue sharing by the Federal Government, provision for crediting local taxes against

amounts due state or Federal governments, and transfer of responsibility for some services to state government, for example. But none of the solutions will be easy or costless. Moreover, if they are to be effective, they must be planned and appropriately timed to meet deficits as they arise.

The deficit projected for the 1975 fiscal year is large, but not nearly so large as the cumulative total of deficits that could occur between now and 1975. Budgets for the coming year probably will have a moderate amount of red ink, with the shade deepening for later years. Next year's problems allow little time for planning. But, hopefully, an early start on the fiscal problems of later years will help head off increasing deficits.

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## INTRODUCTION

This Appendix contains a more detailed discussion than that given in the text of projections made for the different spending and revenue categories of the City and School District. For each element, three different projections relating to possible economic and social conditions in the future are described. Generally, the high projection involves strong economic conditions, rapid inflation, and high social tensions. These conditions would cause the most marked run-up in public spending and revenues. The medium projection, corresponding to a strengthening in economic conditions from their current level, with slowing in inflation, and unchanged social conditions is most likely. Finally, the low projection assumes a weak economy, a substantially reduced rate of inflation, and some easing in social tensions. These conditions would slow growth in spending but have a smaller impact on growth of revenues.

Together, these projections describe a range of revenue and expenditure levels within which actual spending and receipts are likely to fall. It is our conclusion that the middle projection is most probable, while the high and low projections are, indeed, extreme.

The projections are not predictions. According to its Charter, government in Philadelphia cannot run up an operating deficit. Thus, deficits projected here will obviously be wrong. The projections are not intended to be right, but to be a description of the size of the problems that the City and School District may have to face in future years.

### FEDERAL RESERVE BANK OF PHILADELPHIA

## INFLATION IN COSTS OF PUBLIC SERVICES

Inflation is measured in a different manner in the public sector than in the private sector of the economy. Inflation is, by definition, the rise in price of a given product or service—the increase in the price of shoes or of a haircut, for example. In the private sector, all products or services have a price, and although quality changes in products complicate the problem, price changes can be observed and recorded. The products and services produced by government, in contrast, generally have no established price. No price is quoted for the service of having a fire extinguished, for example. Inflation, therefore, must be measured in different ways than it is in the private sector. The established method is to keep track of the cost of things government buys from the private sector and to assume that an expansion in their prices causes a proportionate rise in costs of output of the public sector.

All government costs may be traced back to purchases from the private sector—back to purchases of labor, materials, and services. These items compose the inputs to government. Thus, government inflation is measured by the movement in prices of its inputs, or purchases, while inflation in the private sector is measured by the movement of prices of its outputs or sales. One complication that results from this approach is that improvements in productivity are not taken into account in the public sector. In most private firms, the increase in cost of inputs

exceeds the increase in price of outputs by some amount, averaging about 2 per cent annually. This difference is caused by technological change, learning by workers, and other improvements that raise the productivity of inputs. Since neither prices nor amounts of output by government can be measured and compared to amounts of input, improvement in productivity in government cannot be measured. Thus, to the extent that some improvement in productivity occurs in government, the input-based index of inflation overstates inflation in government. The amount of error is probably small, however, and causes an overstatement in the rate of public inflation of no more than two percentage points annually.

Several different input-based indices, reflecting different rates of inflation in the various sections of City and School District government, have been used in this study. The four major indices are shown in Table 1. Each was projected by combining wage gains already specified in contracts between local government and its workers with projected national price increases in the public sector. The national projections were a product of the Wharton Econometric Model and are consistent with the three levels of inflation of consumer prices shown in Table 1.

## CITY EXPENDITURES

The financial structure of the City includes a large number of separate funds from which appropriations to support each department are drawn. The largest fund, the General

TABLE 1  
PRICE INDICES

	1965 to 1970 ACTUAL	Average Annual Rate of Change 1970 to 1975		
		HIGH	MEDIUM	LOW
Nonuniformed Departments	8	12	10	8
Uniformed Departments	9	13	11	9
School District	10	12	10	8
Philadelphia Consumer Price Index	4.3	5.5	4.5	3.5

Fund, includes the receipts and disbursements of all local taxes and miscellaneous revenues, plus the principal quantity of intergovernmental revenues received by the City. This fund, together with the Capital Fund, contains essentially all the money over which City Council can exercise discretion. Other major accounts—Sewer Fund, Water Fund, Liquid Fuel Tax Fund, Gasoline Tax Fund, and Port Facilities Fund—are for specialized purposes and are only indirectly affected by decisions of the City's governing bodies.

The projections here correspond to expenditures from the General Fund and the interest cost paid from the General Fund to the Capital Fund. Contributions to operating departments from funds over which the City's governing bodies have little direct authority have been subtracted. For example, contributions from the fuel tax and parking funds to the Streets Department have been eliminated. In addition, other units, such as the Model Cities Agency, that are completely supported by special nontax revenues or by intergovernmental aid not included in the General Fund have been omitted. In sum, the projections are restricted to those City expenditures that may impinge upon the local tax base.

The departments for which expenditures have been projected, the revenues they received from the General Fund in the 1970 fiscal year, and their projected appropriations from the General Fund in fiscal 1975 are listed in Table 2. Expenses of nine individual departments which account for 82 per cent of City expenditures, have been projected separately. The 34 smaller City agencies, which spend the remaining 19 per cent are projected in one miscellaneous grouping.

#### COURTS AND LEGAL SERVICES

The court system in Philadelphia came under heavy criticism in the early 1960's as its backlog of cases grew and standards of performance slipped. In 1965, for example, the average criminal case took nearly ten

months for completion, while the larger civil cases took more than four years for decision. Long delays are costly for parties involved in disputes. But perhaps more important, the delays discouraged proper exercise of responsibility by the courts. Many prosecutors watched their cases dissolve during the long wait as witnesses became forgetful or inaccessible. And the hopeless wait for a civil hearing discouraged a number of litigants from ever entering their cases in court.

Philadelphia courts are under the direct authority of the Commonwealth. The Commonwealth amended the Constitution in 1968 to reorganize the Philadelphia courts. Qualifications of judges in the lower courts were raised, and the whole structure was streamlined. These alterations, combined with a sharply increased staff of prosecutors in the District Attorney's office, cut delays in criminal proceedings by half. Long waits in major civil cases remain, however.

These and other changes have meant sharply increased expenditures for Courts and Legal Services in the last three years—up 33 per cent since 1967. The next few years will see further changes in the court system. These alterations, combined with increasing rates of crime, spell continued expansion in spending.

Changes in the way the court system processes cases may lower the system's load below what it otherwise might have been. But improvement in the quality of treatment given cases that do remain in the courts will probably pick up any slack that develops. Consequently, the most reasonable expectation may be that future growth, net of inflation, in the City's expenditures on the Courts and Legal Services will increase at about the rate it has over the last four years—3.5 per cent per year. Any significant attempt to reduce the backlog of cases will increase this expenditure and raise the rate of increase of expenditures on the legal system to perhaps 5 per cent. Finally, if the method of handling defendants is altered and ways of

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treating cases that do reach the Courts stay the same, increases in expenditures on Legal Services would be lower—approximately 2.3

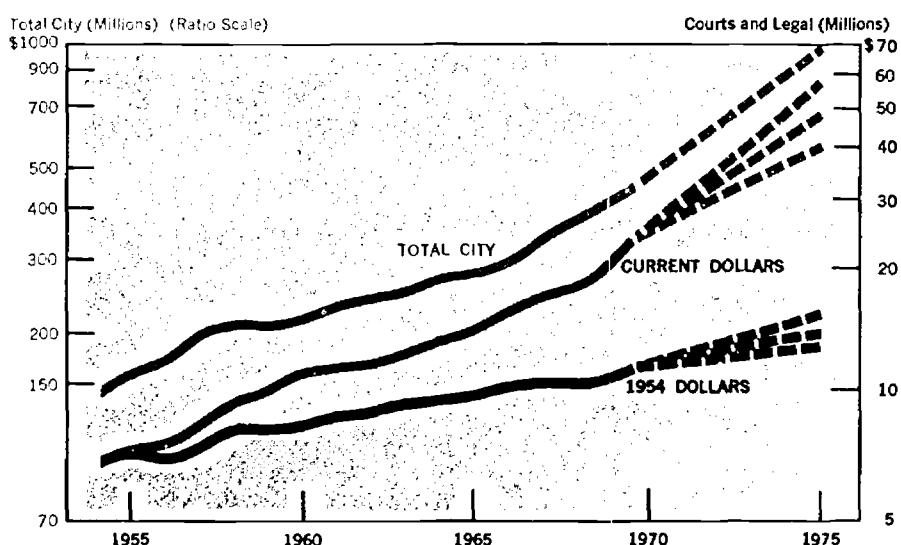
per cent per year. These projections, including the impact of general government inflation, are shown in Chart 1.

TABLE 2  
CITY EXPENDITURES  
(millions of dollars)

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
<b>Constant (1968) Dollars</b>				
Courts and Legal Services	21	28	26	24
Debt Service	52	76	76	71
Fire	26	27	27	27
Health and Philadelphia General				
Hospital	40	71	65	53
Pension and Employee Welfare	38	97	70	41
Police	66	98	89	84
Recreation	29	36	33	31
Streets	35	44	44	39
Welfare	35	48	46	39
Other	64	93	86	74
Total*	406	618	562	485
<b>Current Dollars</b>				
Courts and Legal Services	23	58	48	40
Debt Service	59	102	102	95
Fire	30	61	54	48
Health and Philadelphia General				
Hospital	45	148	121	88
Pension and Employee Welfare	43	152	111	66
Police	80	218	175	148
Recreation	32	74	62	52
Streets	40	91	81	64
Welfare	39	101	85	64
Other	72	194	160	122
Total*	465	1200	1000	787

\* Totals may differ from addition of columns because of rounding.

**CHART I**  
**COURTS AND LEGAL SERVICES**



This category includes expenditures by courts (71 per cent of total group expenditures), District Attorney, Sheriff, Register of Wills, Prothonotary, and fees for witnesses and jurors. Statistical analysis was made of the relation between real growth in expenditures of this category and several other variables, such as crime indices, population, and income of city residents. Results were poor, probably because the appropriation of the unit is determined administratively without the aid of obvious measures of the demand for its services. The final projections, listed in Table 3, were made by extending the trend in spending of the group, with small alterations to represent the effect of changes in methods of handling cases in the courts.

**TABLE 3**  
**COURTS AND LEGAL SERVICES**  
(millions of dollars)

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
Constant (1968) Dollars . . . . .	21	28	26	24
Current Dollars . . . . .	23	58	48	40

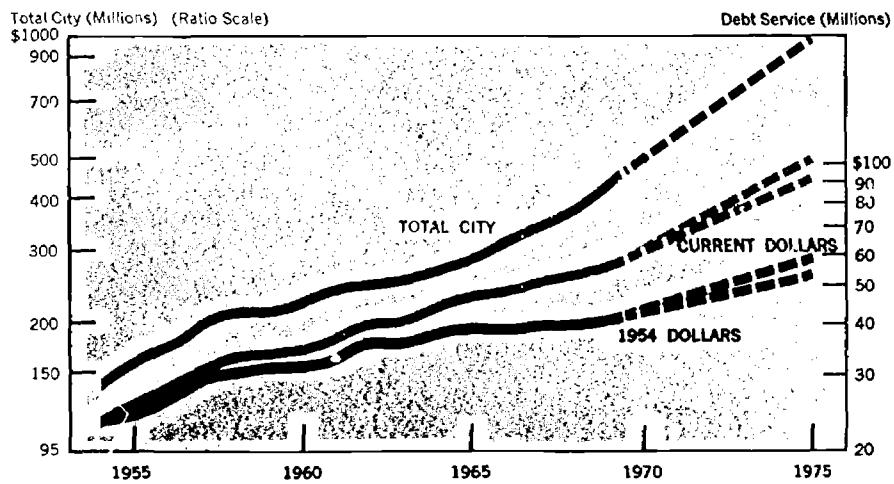
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**DEBT SERVICE**

Construction administered by agencies of the City of Philadelphia is supported, in part, by debt service payment; from the General Fund, including interest and principal on bonds plus down payments on new projects. But General Fund payments for debt service, based on local tax and nontax receipts, are only a part of the money that flows into public construction in Philadelphia. Over the last five years, City agencies have administered \$1.5 billion worth of construction. Three-fifths of this amount was supported by aid from other governments. Of the approximately \$500 million of locally supported construction, \$200 million was supported by payments of debt service from the Sewer and Water Funds. The remaining amount, about \$300 million, was supported by payments of debt service from the General Fund.

Because other funds played a large role, construction administered by the City during the late 60's caused only a small increase in debt service payments financed out of general revenues in Philadelphia. The increase, 20 per cent, was barely more than the growth of inflation over the period. Consequently, when the impact of inflation is removed from the City's payments of debt service, costs to the City are shown to have edged up only slightly.

The slow growth in the cost of debt service to the City will be increased in the next five years, but largely without pressure on the City's tax base. Planned new projects that must be supported by General Fund payments will add up to an 8.3 per cent rate of increase in debt service. (See Chart 2 and Table 4.) However, the projects are concentrated among self-supporting facilities—major new improvements at Philadelphia International Airport and improvements to the City's transit facilities. Rising contributions out of the General Fund, therefore, will be offset by increasing revenues resulting from the new capital facilities.

**CHART 2  
DEBT SERVICE**


Two estimates were made of future debt service payments. The low estimate was based upon the 1970-75 Capital Program of the City. The higher estimate is based on an extension, in constant dollars, of the 1970 level of the City's capital budget to future years. Examination of past Capital Programs showed a slight tendency for the City to underestimate construction in the final years of the Program. Assumption of a constant level of capital spending was used to correct for this.

The constant dollar estimates of construction were translated into current dollar estimates by applying an inflation index for public buildings. Interest costs for supporting the construction were held at a level of 7 per cent. The resulting estimates are shown in Table 4.

**TABLE 4**  
**DEBT SERVICE**  
(millions of dollars)

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
Constant (1968) Dollars	52	76	76	71
Current Dollars	59	102	102	95

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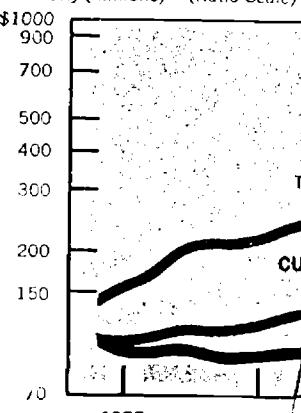
### FIRE DEPARTMENT

largely because the physical size of the City has not changed, Fire Department expenditures have expanded only slightly, after the effects of inflation are removed. One fiscal consequence of this has been a steady decline in the share of General Fund expenditures taken up by the Fire Department—from a little over 10 per cent in 1954 down to 6.5 per cent in 1969.

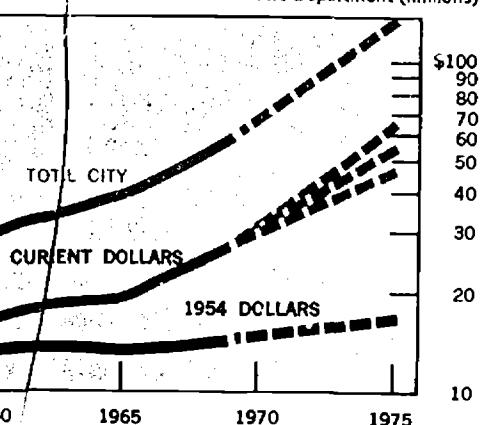
About 97 per cent of the Department's budget goes for putting out fires. The remainder is used for inspection and public education. Fire fighting is carried out by men from 91 fire houses throughout the city. Generally constructed near the turn of the century, many of the fire houses are themselves only marginally above the standards of construction the Department's inspectors require for residences and offices of the city. Ten houses were overhauled in the last five years, and even more will be revamped during the next five years. Expansion in the number of houses, however, which is the main way new capacity is added to the Fire Department, has been limited. During the next five years, only two houses are scheduled for construction. The new staffs of these fire houses, numbering 48 firemen of various grades, is expected to comprise the majority of expansion in the Fire Department. Also, small expansion in the central administration of the Fire Department may be required to coordinate these new facilities. Projections for the Fire Department, combined with expected inflation, are shown in Chart 3.

**CHART 3  
FIRE DEPARTMENT**

Total City (Millions) (Ratio Scale)



Fire Department (Millions)



Real expenditures of the Fire Department were projected by adding to current staff of the Department the expected number of employees of two new fire stations. Each new firehouse, it was assumed, would be staffed with one fire captain, two fire attendants, and 21 firemen, about the average for current houses. It was further assumed that ten more civilian employees would be hired for central administration. Expenditures on items other than personal service are small—8.5 per cent of the fire Department budget. These other expenditures, it was assumed, would not increase in the next five years.

Two different indices of inflation were combined to project current dollar expenditures of the Fire Department. The first measure, for members of the Fire Fighters Union who comprise 97 per cent of employment in the Department, was the wage index computed for the police. Over the years, the Fire Fighters Union has kept salary levels proportional to those of the Police Department. The second, for the small number of civil service employees of the Department, was the index for nonuniformed employees of the City.

**TABLE 5  
FIRE DEPARTMENT  
(millions of dollars)**

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
Constant (1968) Dollars .....	26	27	27	27
Current Dollars .....	30	61	54	48

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**PENSIONS AND EMPLOYEE WELFARE\***

This category is composed, principally, of City contributions towards pension and Social Security plans for its employees. The smaller, nonpension, part of the budget supports insurance and other benefits.

Pension payments have shown dramatic growth in recent years for three reasons. First, the City has, with Court motivation, begun a systematic program of paying off its unfunded actuarial debt (explained below). Second, the pension benefits provided by the City have been substantially liberalized. Finally, recent rapid growth in wages has led to proportional growth in the City's pension contributions.

The pension fund is supported largely on a pay-as-you-go basis by contributions from the City, and by smaller contributions by the Commonwealth and by City employees. In recent years, there has been an effort to increase the balance in the fund to pre-pay pension liabilities and to add a sizable interest income to the sources of pension support.

If the pension system were run as an insurance company would run it, the fund would show a balance at all times that would be sufficient, with its interest income, to pay pensions for which the City were currently liable. The current liability is the sum of pension payments that, given normal lengths of life, must be paid to those currently retired or disabled, plus the pension amounts to which current employees would be entitled. The sum of money required to cover this "actuarial liability" is quite large—about \$550 million in 1967, the last time of evaluation. With a fund balance of less than \$50 million, the amount of money set aside by the City has fallen far short of the actuarial liability. The difference, about \$500 million, is the unfunded actuarial liability. The City

\* We would like to thank Lennox Moak for pointing out the importance of this budget element. Any errors in its projection are, of course, our own.

### Pensions and Employee Welfare (cont'd)

has begun a process of paying off this liability, and this program will add to future pension payments. The amount paid in the 1975 fiscal year will be about \$12 million, up from just \$7 million presently.

More expensive, however, may be the results of the next actuarial evaluation. The City is required to have an actuary compute its liability, and necessary rate of payments at frequent intervals. The next such evaluation will come before 1975 and may substantially increase payments required for new pension liabilities.

The City takes on new liability each working day as more employees are added, average wages are increased, and employees put in more service for the City. As well as paying off the past unfunded liability (the \$500 million), the City attempts to set aside an amount that will cover new liabilities it assumes. The amount that must be set aside is affected by several factors, the most important of which is the expected future rate of growth of average wages. The last evaluation showed that the City must set aside an amount equal to 10 per cent, including payments for Social Security, of its wage payments. This proportion was based on an expected rate of growth of wages of 3 per cent. An increase in this expected rate of wage growth, say to 6 per cent, would about

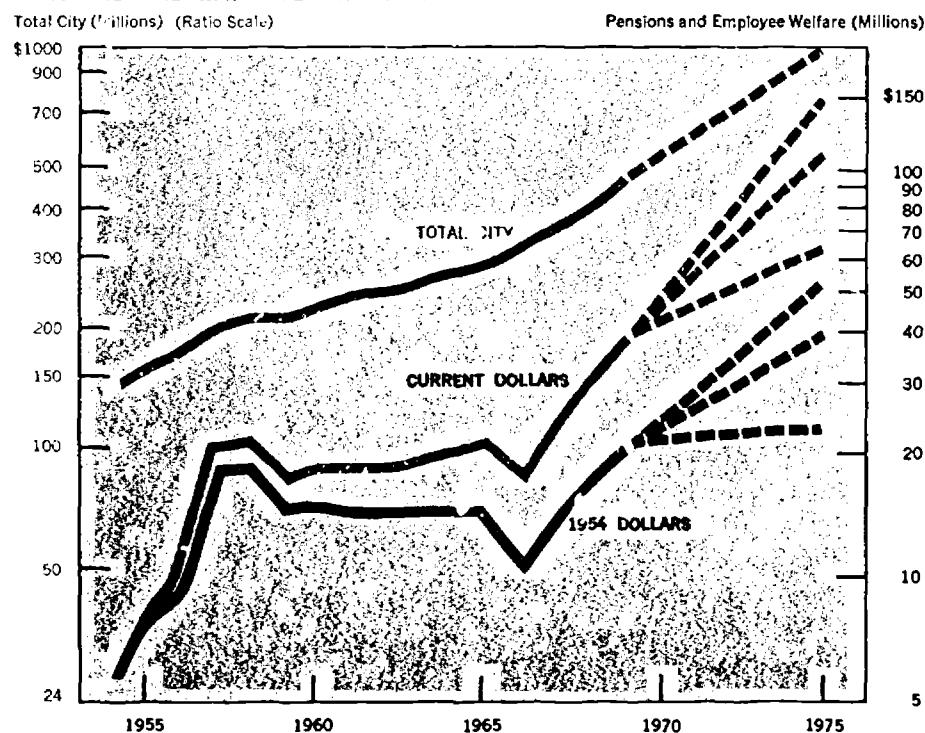
double the percentage contribution required by the City. When the next evaluation is made, a larger rate of wage expansion will be assumed, thus increasing the City's contribution. The exact consequence of this evaluation cannot be known in advance. In these projections, we have assumed three alternative possibilities. On the low side, we held the rate of contribution by the City unchanged. For a medium, and more probable, estimate, we assume that the rate of contribution is increased to 17 per cent. Finally, as a high estimate, we assume a contribution rate of 22 per cent.

Some increase in payments for insurance and other services that make up Employee Welfare will occur. Increase in this element, averaging 16 per cent annually since 1955, has been erratic. We have assumed a conservative growth in this element of 2.4 per cent annually.

Since pensions are a payment by government instead of a purchase of a good or service, the input-based price indices used throughout this study do not apply. All projections were made in current dollars. The constant dollar projections shown in Table 6 are based upon the average price inflation for all of Philadelphia government and are for purposes of comparison with other projections only.

FEDERAL RESERVE BANK OF PHILADELPHIA

**CHART 4  
PENSIONS AND EMPLOYEE WELFARE**



**TABLE 6  
PENSIONS AND EMPLOYEE WELFARE  
(millions of dollars)**

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
Constant (1968) Dollars .....	38	97	70	41
Current Dollars .....	43	152	111	66

## POLICE DEPARTMENT

As crime on the streets has risen, the effectiveness of the Police Department has become a predominant interest of residents of the city. Expenditures reflect this concern. Not only has the proportion of the City budget devoted to police expenditures increased in every year over the last decade, but also it has increased more rapidly than any other component, except pension payments. While inflation in wage levels of police employees has contributed most of the increase, the City has also supported a regular increase in the size of the force.

In the period from 1954 to 1969, the average salary of a policeman in Philadelphia doubled. And, if the trend established in negotiations for the years 1968 through 1971 continues, the average wage level of personnel in the Police Department will double again by 1977.

Salaries of policemen grew more slowly than those in the rest of the economy during the middle 1950's. Moreover, police salaries in Philadelphia fell substantially below those in other large cities during the same period. Ground lost in the 1950's has been amply recovered, yet the determination of police for salary improvements may continue to be strong. At the extreme, salary increases consistent with those in the last three years may continue to 1975. This would mean a two-thirds jump in wage levels by the 1975 fiscal year. More likely, the budget stringency of the City will cause some retrenchment to a rate more consistent with that of the labor

force in the private sector.

Public concern over crime has been translated into higher wages more than into expansion in the size of the police force. The number of policemen per capita has grown at a regular pace over all of the last fifteen years, except for a small jump in 1965.

While the size of the force has increased only slowly, rates of reported crime have jumped sharply. But crime rates are an unreliable measure of the demand for police services. Published crime rates include only crimes reported to and validated by the police. Subtle changes in behavior of the public or in the administrative treatment of crimes may lower or raise the number of crimes reported and validated. For example, a drop in minor crimes in Philadelphia in the last few years was caused, in part, by a change in the method of treating drunks and vagrants. Instead of being arrested as committers of crime, as in the past, drunks and vagrants have increasingly been held in custody with no arrest.

Future years probably will entail growing crime rates. However, the increase in crime need not lead to a proportionate expansion in the number of police personnel and size of expenditures. Expansion in line with that of recent years may be more likely. (See Chart 5.) Our middle projection is an extension of growth in the last four years. The higher projection assumes a significant acceleration in crime combined with an increase in the revenues available to the city for crime fighting. Finally, the lower projection assumes very low growth in crime and budget stringency.

FEDERAL RESERVE BANK OF PHILADELPHIA

**CHART 5  
POLICE DEPARTMENT**

Total City (Millions) (Ratio Scale)

\$1000

900

800

700

600

500

400

300

200

100

0

72

1955

1960

1965

1970

1975

TOTAL CITY  
CURRENT DOLLARS

1954 DOLLARS

Police Department (Millions)

\$200

180

160

140

120

100

80

60

40

20

Extended statistical analysis was made of police expenditures, relating the size of the budget to crime rates, population, personal income, and the total City budget. The final equation used relied upon just one variable, personal income of Philadelphia residents. The equation may be thought of as representing the propensity of Philadelphia residents to consume police services. The results of the statistical analysis were augmented by a projection of crime, traffic duties, and community liaison work. These projections, based upon assumptions about social conditions in the city, were used to increase and decrease projections based upon personal income of residents of the city. The resulting projections are shown in Table 7.

**TABLE 7  
POLICE EXPENDITURES  
(millions of dollars)**

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
Constant (1968) Dollars . . . . .	66	98	89	84
Current Dollars . . . . .	20	218	175	148

### PUBLIC HEALTH DEPARTMENT AND PHILADELPHIA GENERAL HOSPITAL

Changing attitudes towards medical care combined with shifting composition of the city population have increased the responsibility of City government for health services. Medical care has long been considered a necessity—a service that should be provided regardless of ability to pay. But recent legislation, such as Medicare, has helped make this notion fact. Also, multiplication of the city's low-income population has upped demand for local health care. Partially because of these factors, City expenditures for health services, net of inflation, have grown about 6 per cent annually over the last five years. Increased attention to the special medical problems of the population of low-income areas will probably lift this rate of growth to about 10 per cent in the future.

Of course, City health agencies do more than prescribe pills and take heart beats. Dense development of the city requires maintenance of strict standards of sanitation, a livable environment, and a careful watch for communicable disease. But traditional health care at Philadelphia General Hospital and in the many clinics of the Community Health care division of the Department still commands more than 90 per cent of City health resources.

State and Federal governments have increased their aid to Philadelphia for health services. In the 1950's, support for the Health Department and Philadelphia General Hospital derived exclusively from local sources. In contrast, State and Federal governments now provide about 40 per cent of the funds

FEDERAL RESERVE BANK OF PHILADELPHIA

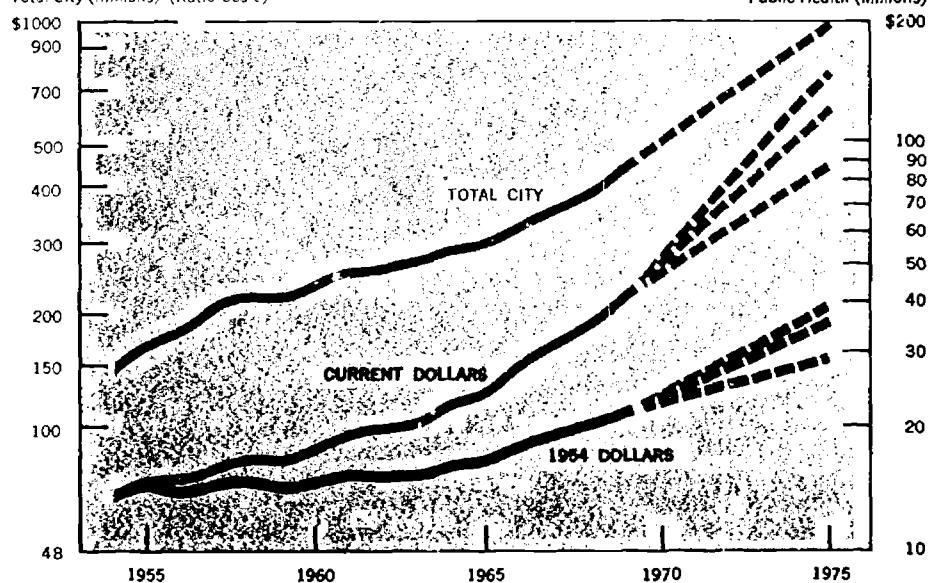
to support these agencies. In fact, no growth would have occurred, after allowing for inflation, had it not been for State and Federal grants. In other words, the real contribution of the City has been essentially constant for ten years. Indeed, more recently, the City's real contribution to these agencies has even declined.

As other governments evidence a willingness to shoulder more of the burden, the City may decide to reduce its load. Our projections reflect two different rates of increase of intergovernmental aid for health and three different responses by the City. The combination yielding the highest growth assumes intergovernmental aid for health will grow by 21 per cent annually, as it has in the last five years, and real City contributions to health care will remain constant. A middle alternative includes the same rate of growth of intergovernmental aid, but a substitution of intergovernmental money for City money

—each dollar of new intergovernmental aid causing a 17 cent reduction in City payments, net of inflation, as it has for the last four years. Finally, the lowest growth would result from a reduction in the trend of intergovernmental aid for health to 15 per cent annual growth, and an increased substitution by the City, to a 25 cent reduction in City contribution for each new intergovernmental dollar.

Other elements in the health category—Medical Examiners Office, Air Pollution and Environmental Hazards Control, and general administration—comprise only 7 per cent of health expenditures and have erratic growth. Real spending for the Examiner's Office is expected to keep up the trend established during the 1960's of 2.7 per cent annual growth; Pollution and Hazards Control spending is expected to remain constant in real terms; general administration expenditures are expected to grow in proportion to total health spending.

**CHART 6**  
**PUBLIC HEALTH DEPARTMENT AND PHILADELPHIA GENERAL HOSPITAL**  
Total City (Millions) (Ratio Scale)



**TABLE 8**  
**PUBLIC HEALTH AND PHILADELPHIA GENERAL HOSPITAL**  
(millions of dollars)

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
Constant (1968) Dollars	40	71	65	53
Current Dollars	45	148	121	88

FEDERAL RESERVE BANK OF PHILADELPHIA

**PUBLIC WELFARE**

Higher crime rates and an increase in low-income households in Philadelphia both put pressure on the Department of Public Welfare. As well as carrying out the City's responsibility to the physically and fiscally indigent, the Department watches over the care and rehabilitation of persons imprisoned through arrest or through conviction in Philadelphia courts. Reflecting increasing importance of these concerns in the city, the share of the total City budget going to the Department has constantly increased.

**Child Care.** Responsibility for administering welfare services in Pennsylvania is split between the Commonwealth and local governments: the Commonwealth shoulders the heavy burden of payments to needy families; Philadelphia's responsibility is for institutional care of neglected, dependent, or delinquent children, and aged or infirm adults. Care of children, consuming about 60 per cent of welfare money, is the largest welfare function of the City and accounts for an overwhelming share of past and future expansion in welfare costs.

Two factors account for the increasing importance of child care. First, while numbers of City recipients in other categories have been declining, the number of children under care has risen sharply. The sharp rise in children under care reflects the change in composition of the city's population—towards more low-income families.

A second cause of the increasing importance of child care is expansion in cost of treating each child. In the early 1960's, private voluntary agencies provided substantial savings to the City by administering much of the child care. However, as the number of children under care mushroomed beyond the capacity of private agencies, the public role expanded. Since taxpayers must bear the full cost of treatment when it is provided publicly, the average cost per child to the City naturally grew.

As the low-income population of the City continues to grow, the number of children under care probably will continue to grow—perhaps by about 13 per cent to fiscal 1975. With much of the change in responsibility for administering child care now completed, the growth of cost per child may slow. We have taken that as a minimum projection. More likely, there will continue to be increases, between 4 and 7 per cent annually, to support improved quality of care.

**Care of the Aged.** The Department of Public Welfare provides care for the aged principally through the Riverview Home. Riverview, once regarded as essentially a rest home, has in recent years been upgraded to provide full nursing home facilities. The increased medical care implicit in this change, of course, has meant a sharp increase in cost per patient, as well as reduction in the number of patients served by the facility. Between 1966 and 1968, the real expenditure per patient more than doubled, while the total number of persons served within the facility decreased by 15 per cent. The resident population of the home has now stabilized at a level of 850, with a number of outpatients. Costs, however, may be expected to continue to rise as further improvements in medical services are made in future years. The exact jump in costs will largely depend upon budget stringency of the City. As a minimum, we have projected a standstill in expenditures per patient, with future growth of from 3 to 6 per cent annually more likely.

**Custody of Prisoners.** Despite rapid increases in crime, the prison population for which Philadelphia provides support has declined continuously over recent years. Two forces underlie change in the number of inmates. First, the courts have lowered the relative number of prison sentences they deal out. They have substituted parole and probation for time behind bars. Second, as

changes in the bail system have made bail more accessible to low-income persons, growth in the numbers temporarily held in custody before trial has slowed.

The most substantial change in the future probably will be in the number of persons held awaiting trial. Programs tried or discussed at present, including substitution of cash bail for the current bail-bond system, or pre-indictment probation, may ultimately reduce the number of detainees by as much as 50 per cent.

Adding up these possibilities, the lowest expenditure projection is that current programs would be successful in emptying City jails of as many as half of their detainees by 1975, that the courts would continue their practice of dealing non-jail sentences, and that the increase in crimes would be low. This combination would yield a small reduction in prisoners in State institutions—of about 15 per cent—and a larger reduction in the City prison population—30 per cent. More likely, courts will deal out somewhat stiffer sentences as pre-indictment probation reduces the caseload of the courts, and as they try an increasing number of cases. This may yield an approximately stable population in State prisons and a slight decline in the City prison population—5 per cent. Finally, a rapid increase in crime within the city, combined with stiffer treatment in the courts, would increase the population in both the State and City prisons—by approximately 20 per cent and 10 per cent respectively.

Expenditures per prisoner have risen rapidly in recent years. This increase reflects an upgrading of care and the tendency for many prison costs to be unaffected by decline in the number of inmates. The fluctuation in total costs is not completely proportionate to the number of prisoners in institutions. Indeed, total real expenditures for Philadelphia prisons have been almost constant up to the last couple of years, while the number of inmates has varied widely. The lower estimate of prison population may

FEDERAL RESERVE BANK OF PHILADELPHIA

lead to a rise of about 25 per cent in expenditures per prisoner—reflecting fixed costs and maintenance of current standards of services. The medium and high estimates of prison population are consistent with continued small increases in costs per prisoner

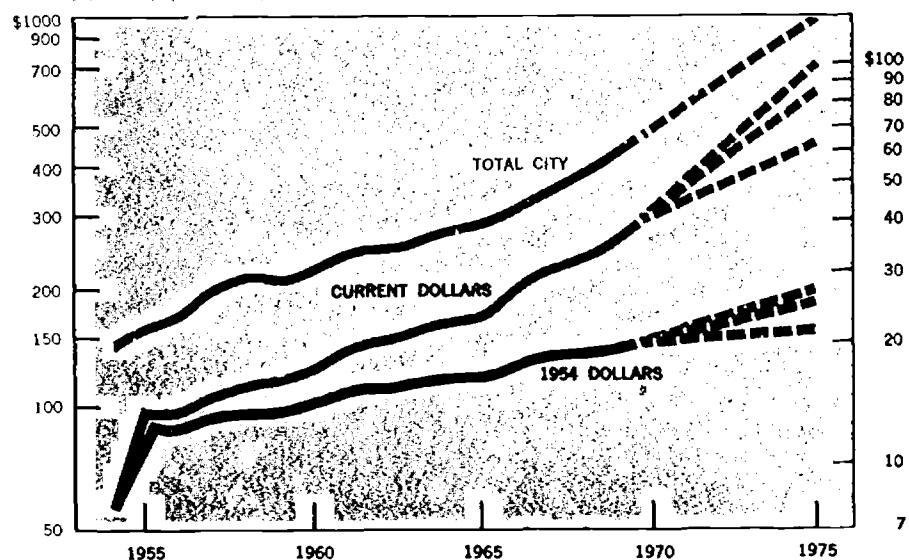
as the quality of the correctional system is upgraded.

Total expenditures and projections for prisons, the Riverview Home, child care and other duties of the Department of Public Welfare are shown in Table 9.

**CHART 7**  
**PUBLIC WELFARE**

Total City (Millions) (Ratio Scale)

Public Welfare (Millions)



**TABLE 9**  
**DEPARTMENT OF PUBLIC WELFARE**  
(millions of dollars)

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
Constant (1968) Dollars .....	35	48	46	39
Current Dollars .....	39	101	85	64

## RECREATION AND CULTURAL SERVICES

This group of activities augments the efforts of other parts of local government in Philadelphia. Expenditures of this group have grown at about the same rate as has the total City budget in recent years.

**Department of Recreation.** This unit specializes in the operation and maintenance of recreation centers, playgrounds, swimming pools, skating rinks, golf courses, and other recreation facilities scattered throughout the city. In the last four years, the number of such facilities has increased by about 5 per cent, and the average amount of expenditure, net of inflation, on service at each facility has expanded by about 10 per cent, yielding a total increase of 15 per cent in real expenditures. Plans for future expansion in facilities, listed in the Capital Program of the City, indicate a much more energetic development of recreation spots in the area. If completed, the plans alone would increase recreation services by 30 per cent, and increase in staff at facilities throughout the city would chalk up another 15 per cent of expansion. This rate of growth is taken as the high rate in these projections; the medium rate is an extension of past rates of building; and the low is that projection implied by no increase in the number of recreation facilities in the City.

Remaining responsibilities of the Department include contributions to private agencies, such as Robin Hood Dell, Incorporated, and the Philadelphia Grand Opera Company; operation of the Veterans' Stadium Complex; and general administration. The new stadium will push these costs up to a higher rate of growth than they have shown in the past—with total spending moving up \$2 million to \$3.5 million in the 1975 fiscal year.

**Fairmount Park Commission.** The Commission is concerned with City appropriations

to the Art Museum, the street beautification campaign, and upkeep of over 8,000 acres of open space. Of the numerous programs under FPC jurisdiction, park patrol is largest in expenditure terms. Yet the patrol has shown little change in the 1960's, and the number of park guards hovers around 525. As traffic and crime become a more important consideration for the Park Commission, some increase in the number of guards may be expected. We have projected a 5 per cent rise in the numbers of guards.

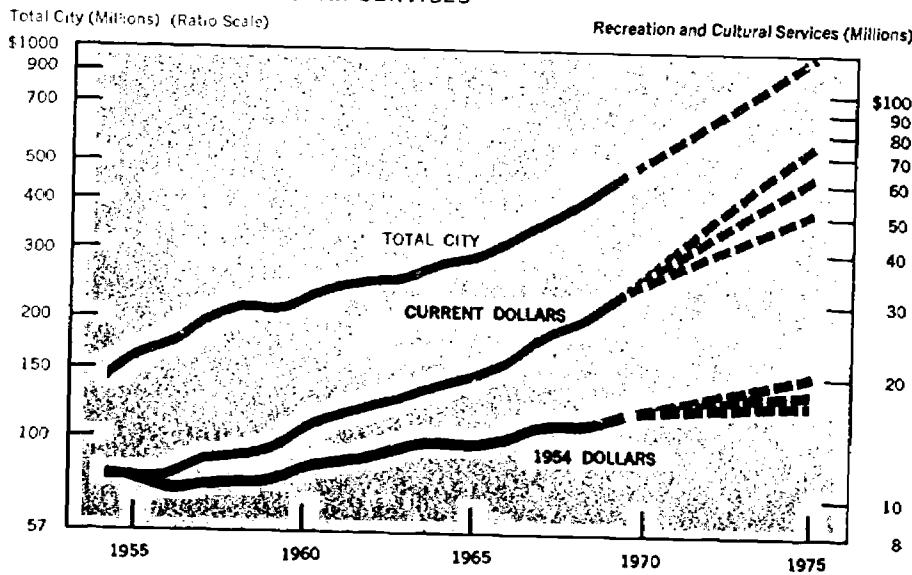
Other programs of the Fairmount Park Commission include maintaining park areas and conducting various recreation programs in cooperation with the Department of Recreation. The maintenance expenditures, which have been essentially constant, net of inflation, in recent years, were projected to remain constant. Expenditures on recreation programs were projected to grow at the rate established for expenditures by the Department of Recreation.

**Free Library System.** The system maintains collections and provides library materials and professional services at the main library at Logan Circle, the Mercantile Library, several special facilities, and 44 branch libraries. Expenditures for these services were projected in two parts. First, the number of new facilities and expansion in personnel required by these facilities were projected. Second, increase in expenditures per facility was projected. Three different levels of expansion of facilities were projected—a high projection, consistent with the Capital Program of the City; a medium projection, equal to an extension of the past trend in the number of facilities; and a low estimate, assuming no new facilities. Expenditures per facility were extrapolated by extension of the past trend.

Combined projections for the Department of Recreation, the Fairmount Park Commission, and the Free Library System are shown in Table 10.

FEDERAL RESERVE BANK OF PHILADELPHIA

**CHART 8**  
**RECREATION AND CULTURAL SERVICES**



**TABLE 10**  
**RECREATION AND CULTURAL SERVICES**  
(millions of dollars)

Constant (1968) Dollars	Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
Current Dollars	29	36	33	31
	32	74	62	52

## STREETS DEPARTMENT

The Streets Department does the City's housekeeping—trash collection, street maintenance, street lighting, and traffic engineering. As a whole, the function has received decreasing attention in recent years, as expenditures, net of inflation, have shrunk by almost 2 per cent per year.

The largest part of this Department's budget is earmarked for sanitation—collection of trash throughout the City. Contrary to expenditures for the whole Department, spending for sanitation has shown a gradual and continuing increase over the years. The main source of the increase has been growth in tonnage collected—a trend that probably will continue. Cost per ton of trash collection, however, has increased only slightly. Sanitation expenditures were projected by assuming a 5 per cent annual rate of growth in tonnage collected and continuation in the slow upward trend in cost of collection per ton.

Maintenance and construction of streets has received very sharp cutbacks in recent years. Worsening conditions of streets will probably cause some expansion in expendi-

tures in the future. The timing of the increase in maintenance, however, is uncertain. Two assumptions were made. The low projection is based on the assumption that maintenance stays at its current level during the next five years. The middle and high projections assume a resumption of the level of maintenance that was carried out in the early 1960's—about 35 per cent above the current level.

About two-thirds of current street maintenance expenditures are supported by gasoline and other fuel taxes not included in the General Fund of the City. Revenue from these taxes was subtracted from the maintenance expenditure for these projections. Since these taxes grow slowly, much of the projected increase in maintenance spending must come from the General Fund.

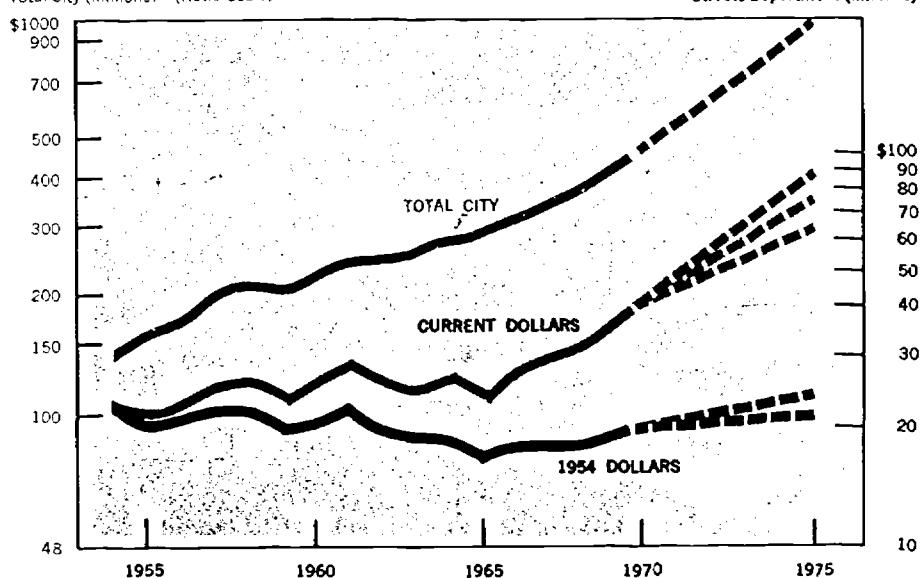
Street lighting and traffic engineering expenditures were both projected to remain approximately constant in the next few years. A slight increase in electricity used for lighting was assumed for medium and high projections. For the high projection of engineering, a resumption of spending at the 1963 level was assumed. Combined expenditures for the complete budget of the Department of Streets are listed in Table 11.

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**CHART 9  
STREETS DEPARTMENT**

Total City (Millions) (Ratio Scale)

Streets Department (Millions)



**TABLE 11  
STREETS DEPARTMENT  
(millions of dollars)**

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
Constant (1968) Dollars .....	35	44	44	39
Current Dollars .....	40	91	81	64

### OTHER OPERATING AND MISCELLANEOUS EXPENDITURES

This category may be broken into seven divisions: (1) Offices of Elected Officials; (2) Supporting Offices; (3) Tax Collection; (4) Commerce; (5) Public Services; (6) Licenses, Inspections and Public Property; and (7) Education Support.

The first, Offices of Elected Officials, includes the Offices of Mayor, of City Councilmen and of City Commissioners—8.0 per cent of "other." Supporting Offices (22.9 per cent) are the following: City Planning Department, Economic Development Unit, Development Coordinator, Redevelopment Authority, Finance Department (excluding Capital Budget Financing), the Managing Director's Office, Auditing, Department of Records, City Treasurer, Procurement, and the Law Department. Tax Collection (11.9 per cent) includes the Department of Collections, the Board of Revision of Taxes, and the Tax Review Board. Commerce (9.4 per cent) takes in the Department of Commerce, the Office

of City Representative and the Philadelphia Civic Center.

The Office of Information and Complaints, the Fair Housing Commission, the Commission on Human Relations, and the Office of Civil Defense all fall into the Public Service category (1.6 per cent). The sixth category includes the Department of Public Property (31.0 per cent), the Department of Licenses and Inspections, the Zoning Board of Adjustment, the Licenses and Inspections Review Board, and the Board of Building Standards (9.8 per cent). The last category, Education Support (5.3 per cent), takes in expenses for the Philadelphia Historical Commission, the Art Commission, the Youth Study Center, and contributions to Community College.

Other Operating and Miscellaneous Expenditures has remained a rather constant proportion of the total budget of the City. Therefore, it was projected as a multiple of the projections made for other City departments—equal to .15 times the total.

FEDERAL RESERVE BANK OF PHILADELPHIA

CHART 10  
OTHER OPERATING AND MISCELLANEOUS EXPENDITURES

Total City (Millions) (Ratio Scale)

Other Operating and Miscellaneous (Millions)

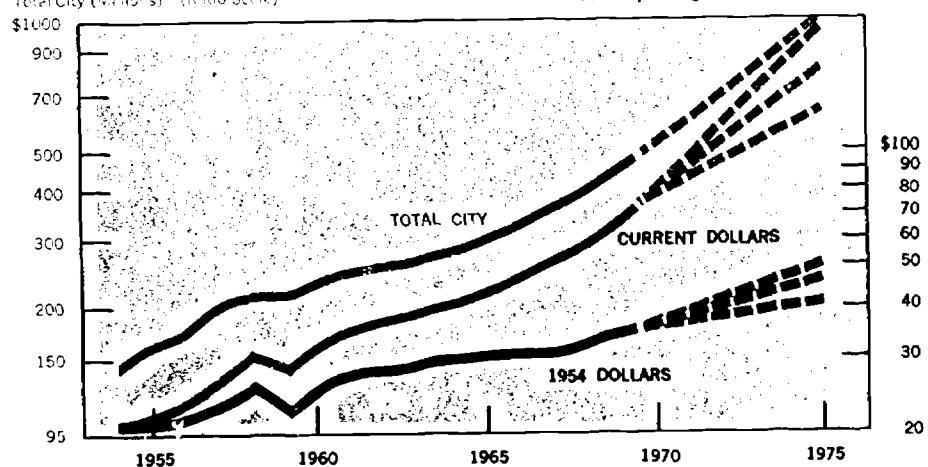


TABLE 12  
OTHER OPERATING AND MISCELLANEOUS  
(millions of dollars)

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
Constant (1968) Dollars	64	93	86	74
Current Dollars	72	194	160	122

## SCHOOL EXPENDITURES

In his introductory message accompanying the 1971 budget, Dr. Mark Shedd, Superintendent of Schools of Philadelphia, described the budget in the following words: "It is a standstill budget from which we have already pared more than \$8 million of vitally necessary services to children and adults. It is a budget that provides very little at a time when much is needed. It is a budget of frustration." In the document, he went on to call for a \$314 million budget, better than 10 per cent higher than the previous year. The discouraging tone used to characterize this sizable increase is indicative of the forces which currently impinge upon the School District. While population in the city has remained nearly constant for the last twenty years, the student body served by the public schools of Philadelphia has grown constantly. Moreover, the composition of the student body served by Philadelphia schools has changed. So the kinds of learning problems with which the School District must deal have changed. The growing student body and changing educational needs have put substantial pressure on the School District to increase quantity and quality of its services. But the schools also have faced successful pressure from their employees for large salary increases. And the static tax base upon which the School District must rely has forced it to increasingly depend for financial aid upon the Commonwealth of Pennsylvania, a government which has had its own share of financial problems.

Despite the fiscal pressures, the School District has continually increased the amount of attention it provides to each of its students. Also, it has developed some new programs to serve special segments of the student body—programs such as Head Start and Follow Through.

The vast majority of School District money, however, has gone to pay for greater amounts of traditional classroom education and the services and facilities that support

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it. In this projection, we have assumed that classroom education will continue to dominate school spending as fiscal pressures restrict the extent the District can diversify.

#### STRUCTURE OF SCHOOL FINANCE

School spending is supported by three main accounts—a General Fund, a Capital Fund, and a Federal and Other Grants Fund. The General Fund, the largest account, includes all local tax receipts, all aid from the Commonwealth of Pennsylvania, and a small amount of Federal aid. The Capital Fund supports the building program and, itself, is supported by payments from the General Fund. Finally, the Federal and Other Grants Fund includes special revenues to support particular programs of the School District, such as retraining of unemployed workers, Head Start, and computer-assisted education.

While some of the programs supported by this Fund may be transferred to the General Fund and thus to the fiscal resources of the School District, most exist only so long as the Federal Government is willing to support them. Consistent with the projections made for the City, we have projected only those spending elements that depend directly upon the tax base of the city—those elements supported by the General Fund. The categories of spending projected, and their projections, are shown in Table 13.

#### GRADE-LEVEL COSTS

**Inflation.** The largest part of recent expansion in the School budget has been caused by pay hikes for District personnel. Starting in the mid-1960's, a series of negotiated contracts between the School Board and the Philadelphia Federation of Teachers established

TABLE 13  
SCHOOL DISTRICT EXPENDITURES  
(millions of dollars)

	1970 Expenditure	1975 Projections		
		HIGH	MEDIUM	LOW
<b>Constant (1968) Dollars</b>				
Administration and				
Miscellaneous	16	24	23	22
Debt Service	26	75	75	75
Elementary Education	103	127	122	117
Secondary Education	102	174	165	156
Vocational and Technical				
Education	6	11	11	10
Total*	253	411	395	379
<b>Current Dollars</b>				
Administration and				
Miscellaneous	18	47	40	34
Debt Service	29	92	83	75
Elementary Education	115	247	213	182
Secondary Education	113	339	288	245
Vocational and Technical				
Education	7	22	19	17
Total*	282	747	643	552

\* Totals may differ from addition of columns because of rounding.

benchmarks for individual wage increases in all job categories. The reference points led to an increase of 27 per cent in the average salary of all personnel in the system during the last three years, with nonteaching personnel receiving somewhat bigger gains than teachers.

The exact path that wages take in the future will be decided in negotiations among workers and the School Board. We have assumed that wage gains for personnel of the District will reflect gains made by other government employees in Philadelphia—continued large increases for a short time, and then some tapering off.

**Employment.** Increase in salaries accounts for about half of recent expansion in the budget of Philadelphia schools. The remainder is taken up by more personnel, materials to support the personnel, and by an expanded program of building. Both the staff expansion and the building program have had the objective of reducing overcrowding in Philadelphia schools. But staff expansion has gone beyond this objective as new types of personnel have been added.

In the last four years, a total of 3,049 new employees, amounting to a staff increase of 16.5 per cent, have been hired by the District. Not quite half of the new staff, 1,300, are teachers. This increase has lowered the average number of students per teacher in the public schools by about 7 per cent. Most of the new teachers work in elementary and junior high schools, where new enrollment has been largest and most new classrooms were added. But a larger part of the staff expansion was in nonteaching positions. These workers, including counselors, supervisors, and teachers' assistants, have been relied upon to help teachers by relieving them of some of their nonteaching duties and by providing curriculum and disciplinary support.

**Cost Per Student.** The increase in personnel has far surpassed growth in the

number of students and thus has added significantly to cost of education per student. About 85 per cent of School expenditures, excluding debt service, go for personnel salaries. The remaining amount, which has remained a stable multiple of the personnel cost, includes purchased services, books, and other supplies. Personnel and other nondebt service costs ranged, in 1970, from \$688 per student for elementary grades to \$1,000 for vocational-technical students. Spending for elementary students was up \$78 from the 1965 level of \$610, net of inflation. A more dramatic increase occurred in spending for secondary students—up \$150 from the 1965 level of \$770, or 20 per cent. (See Chart 11.) The cost of teaching vocational-technical students has ranged between \$1,000 and \$1,100 since 1964.

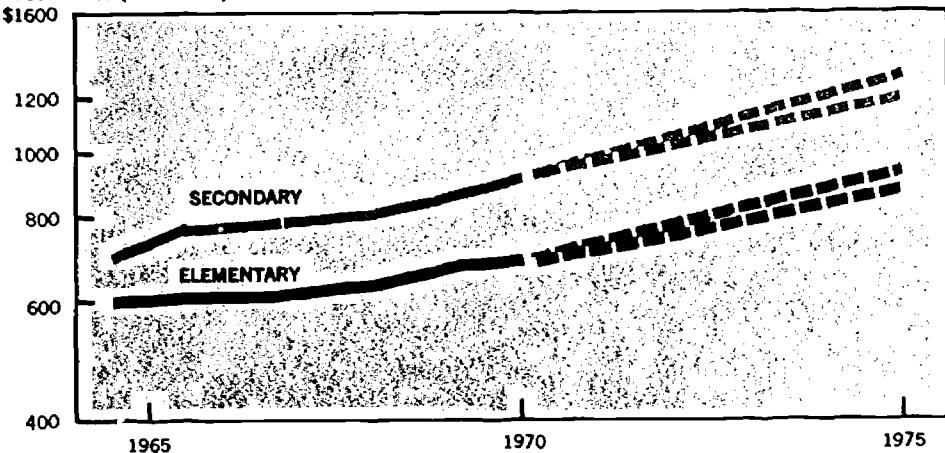
Expenditure per student in 1975—net of inflation—will be a function of ongoing changes in the School Board's goals and policies. Continued decline in number of students per teacher, more support personnel, and increased instructional equipment purchases probably will all add up to higher per student expenditures. As public pressure continues for improved performance in the teaching of basic skills, real expenditure per student very likely will continue to rise.

Increase in expenditures per student was projected by extending the trend in past spending, net of inflation. The high projection is based upon the trend in spending established since 1968. (See Chart 11.) The lower projection is based on the more conservative trend of the years 1964 through 1970. Per student expenditures in vocational-technical schools (not shown on Chart 11) have traced an erratic course in recent years. Since the category is small, it was simply assumed that vocational-technical costs would grow at the rate projected for secondary schools.

**Enrollment.** Over the last ten years, the population of the city of Philadelphia has

FEDERAL RESERVE BANK OF PHILADELPHIA

**CHART 11**  
**COST PER STUDENT**  
**1968 Dollars (Ratio Scale)**



declined by a small amount. The number of children attending public schools in the city, however, has expanded by nearly 20 per cent. The cause is a change in the composition of the population of the city. While many of the white children of the city attend private or parochial schools, most black students attend the public schools. Thus, as the white population of the city has declined, and as the black population has grown, the number of students attending public schools has increased. Witness the shift in composition of enrollment—from 47 per cent black in 1960 to 60 per cent black in 1970.

This increase in enrollment was augmented in the late 1960's by a sizable expansion in the kindergarten program of the District. Of the 14,000 increase in number of students between 1965 and 1970, one-third was in new kindergarten classes. With the kindergarten program now largely filled out, this source of growth will have less impact in the future. In addition, slow in-

migration and low birthrates that reduced growth in total enrollment over the last few years may be expected to have a dampening effect during the early 1970's as well. As a maximum, we project an enrollment expansion of 15,000 between 1970 and 1975. Continued slow growth, however, would result in a student expansion of only about 5,000, which we have used as a low projection. (See Chart 12.)

Increase in enrollment may add from 2 to 6 per cent to School expenditures by 1975. Change in the relative number of students in secondary schools may add another 4 per cent to School costs. Expenditures per student are higher in secondary than in elementary schools, principally because of the wider curriculum of the upper grades. The relatively large expansion in numbers of students in elementary grades that occurred in the late 1960's will mean a bulge in the upper grades in the early 1970's. So, expenditures for secondary schools will be ex-

**CHART 12**  
**TOTAL STUDENT ENROLLMENT**

Thousands

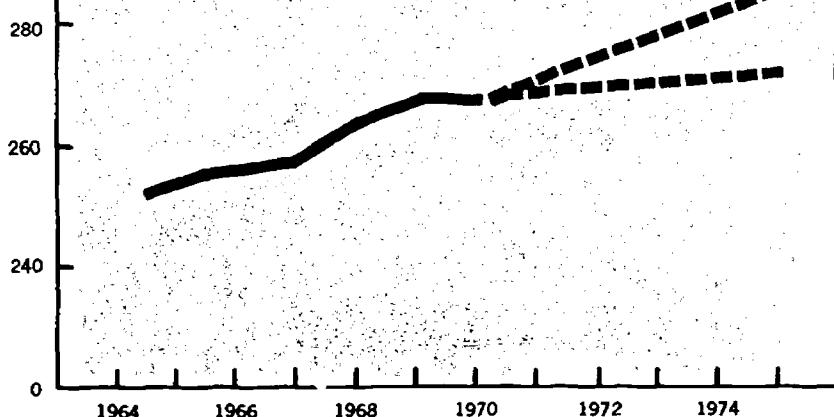
300

280

260

240

0



panded, and the total School budget will be increased.<sup>1</sup> Combined projections, reflecting growth in enrollment and increase in spending per student are shown in Table 13. The miscellaneous category, administration, extension, and other, included in the Table, has been projected as a multiple of the grade-level costs.

#### DEBT SERVICE

Expansion of staff and enrollment of the District has been facilitated by the construc-

tion of new school buildings. And, although rates of construction over the last five years have been high, even greater building efforts are planned for future years. The building program is directly supported by bonds sold by the School District. The annual costs to the School District are payments from the General Fund for interest and principal to retire the bonds.

Annual payment on the outstanding debt has jumped from \$9 million in 1962 to over \$28 million in 1970—an increase of 300 per cent. However, the most significant increases are yet to appear, as principal and interest charges come due on proposed general obligation bonds for the expanded Capital Program. By 1975, debt service may reach \$83 million and absorb 14 per cent of the School District's general fund expenditures, up from the current level of 10 per cent.

<sup>1</sup>Impact of the change in grade-level composition of enrollment is determined by calculating the percentage difference between average cost per student, given the current balance among elementary and secondary students, and the average cost with the expected 1975 grade-level composition.

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This estimate of future debt service is based upon two forms of outstanding debt in 1975—debt from the activity of new school construction and debt resulting from long-term bonds floated during 1970 to bring the operating budget into balance.

Plans for the construction of new schools have been greatly curtailed in the last two fiscal years. The first setback took place in May 1969, when voters defeated a \$90 million bond referendum. Proposed spending was cutback, and a stripped-down version

of the May bond proposal for \$65 million was presented to the voters in November and approved. At the same time, the national economy was going through a period of tight money, and tax-free School District bonds which yield a 7 per cent return were not attractive to investors. Now that market conditions have eased and School District bonds are once again attracting buyers, the 1971 fiscal year will involve catching up on delayed projects. The original capital budget for 1971 scheduled \$25.5 million of new

**TABLE 14  
COMPONENTS OF DEBT SERVICE, 1970 AND A  
PROJECTION TO 1975. THE SCHOOL DISTRICT OF PHILADELPHIA**

Fiscal Year	1970 (millions of 1968 dollars)	1975 (millions of 1968 dollars)
<b>1. Debt Service Resulting From:</b>		
a. Outstanding School Construction Bond Issues as of June, 1970 .....	26	32
b. Outstanding Operating Budget Bond Issues as of June, 1970 .....	0	6
<b>2. Total Debt Service on Outstanding Bonded Debt as of June, 1970 .....</b>	<b>26</b>	<b>38</b>
<b>3. New Debt Service Resulting from Scheduled Appropriations in the 1971-1976 Capital Program .....</b>	<b>0</b>	<b>26</b>
<b>4. Lease-Purchase Payments to the Pennsylvania State Building Authority .....</b>	<b>0</b>	<b>11</b>
<b>5. Total Debt Service on Outstanding and Programmed Debt .....</b>	<b>26</b>	<b>75</b>

Sources:

I. Director of Finance, Treasury Office.

II. School District of Philadelphia, *Annual Financial Report, 1969-70*, p. 23.

III. School District of Philadelphia, *Proposed Capital Budget and Program, 1971-1976*, Schedule II, p. 4. To obtain the \$25,852,000 figure, \$31.7 million (line 1) was subtracted from the total existing and proposed capital debt service level in 1974-75 (Schedule II) of \$57.6 million. All of the School District's programmed expenditures and debt service are in 1968 constant dollars.

spending for school construction. However, \$63.5 million in unused appropriations from the 1970 fiscal year were added to the original 1971 capital budget—bringing the total level of budgeted capital spending in 1971 to \$89 million. Debt service on the bonds issued to finance this spending and all prior capital outlay will be \$32 million in 1975. (See Table 14.)

On top of the debt service for School construction, the Board of Education used its long-term borrowing capacity to balance the 1970 operating budget. The first payment on this \$28 million worth of long-term debt is due in May of 1971. The fifth and final payment will come due in fiscal year 1975. Total principal and interest payment on this operating fund debt in 1975 is \$6 million (Table 14).

Finally, additional capital fund appropriations are planned to complete the School District's long-range school construction program. Initial plans were to finance all school projects through the use of the School District's borrowing capacity and voter referendum. However, with some uncertainty in the bond market remaining, the Board of Education turned to the State School Building Authority as a new source of financial aid for the Capital Program. Since it is not subject to a 7 per cent limitation, the State Authority is in a better position than are local School Districts to generate funds in the bond market.

The State Public School Building Authority as a source of financing is introduced for the first time in the 1971-1976 Capital Program.<sup>1</sup> Over \$122 million in capital expenditures are planned by the Authority between 1970 and 1974. Rental payments on these State-owned projects in 1975, and debt service stemming from construction financed

<sup>1</sup> The Authority will issue its own 30 to 40 year bonds, solicit bids, award contracts for, and supervise construction. The School District will lease the buildings for the life of the bonds before assuming title to the properties.

through new bond issues are shown in Table 14 (lines 3 and 4). Service on current debt—both for construction and operating purposes—plus rent and debt service for new construction may cause growth of almost 180 per cent in total payments.

## CITY AND SCHOOL DISTRICT REVENUES

### FISCAL ADMINISTRATION: CITY

Each year, the Mayor submits a budget proposal to City Council for review and approval. Included in the document is an estimate of revenues available to pay the bills—revenues that mainly come from either local taxes or from intergovernmental aid. The City Council has the power to trim down the Mayor's budget if it thinks spending is too high, or it can hike tax rates and levy new taxes to produce enough revenue to meet expenditures. Often, both procedures are used to balance the budget.

### FISCAL ADMINISTRATION: SCHOOL DISTRICT

The School District, on the other hand, has a more complex fiscal structure. Management of the School District is in the hands of the Board of Education, while authorization to levy taxes in support of education is the responsibility of City Council. Each year, the Board of Education submits a lump sum statement of anticipated revenues and expenditures for the next fiscal year to the Mayor and City Council of Philadelphia, and requests authorization to levy taxes that may balance its budget for the year. Thus, responsibility for the way public education revenues are to be spent (the function of the Board of Education) and responsibility for taxes in support of the spending (the job of City Council) are divided between two different authorities. Consequently, the School District is neither fiscally independent and able to levy its own

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taxes, nor fully dependent upon the City Council in the allocation of the public education dollar.<sup>3</sup>

#### OVERVIEW OF REVENUE PROBLEMS

Historically, Philadelphia depended upon its real property tax for the bulk of revenues to pay the bill for public services. In 1952, the City culled over 40 per cent of its revenues from the real estate tax, while the School District relied on the same tax for 65 per cent of its funds (Charts 13 and 14). However, the connection between revenue from the real property tax and spending for

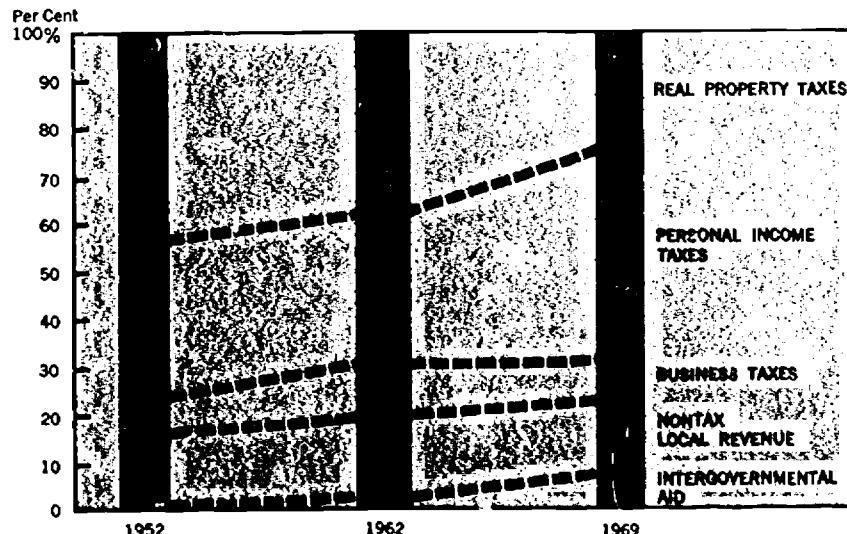
local public services became rocky in the early 1960's. While national and Delaware Valley economies were signaling strong growth, Philadelphia was faced with continued out-migration of firms and of middle- and high-income families. As the demand for residential, commercial, and industrial properties softened, growth in the value of real property began to fall behind expansion in spending on education and municipal services.

The response of City and School District administrators to this eroding tax base reflects two different strategies. Financial planners for the City of Philadelphia turned to a local tax base showing much healthier signs of growth—personal income. While growth of taxable real property had come to a near standstill, wages and salaries of Philadelphia residents have expanded at a pace

<sup>3</sup>The effect of this division of responsibility is essentially a political matter, and was not examined. However, the division may have made the search for a rational solution to the deepening revenue problem even tougher for government leaders.

CHART 13

THE CITY OF PHILADELPHIA HAS INCREASED ITS RELIANCE UPON PERSONAL INCOME TAXES.



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CHART 14  
AND THE SCHOOL DISTRICT HAS TURNED TO  
THE COMMONWEALTH.

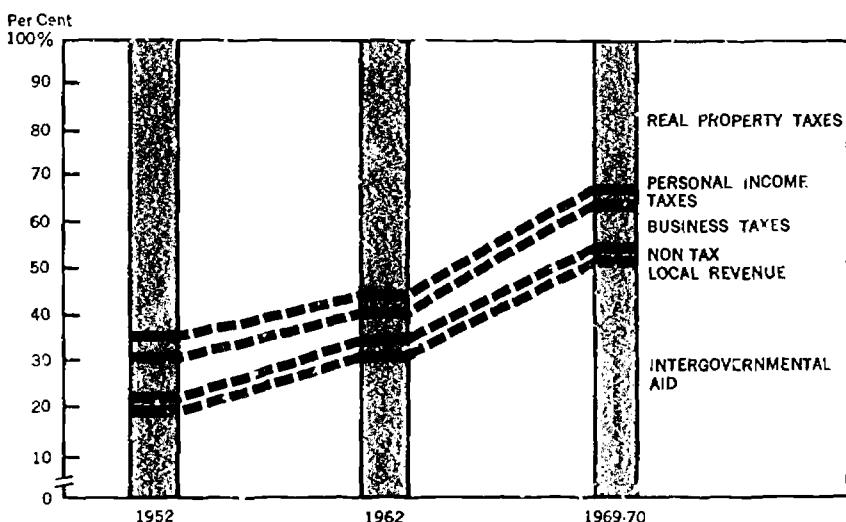
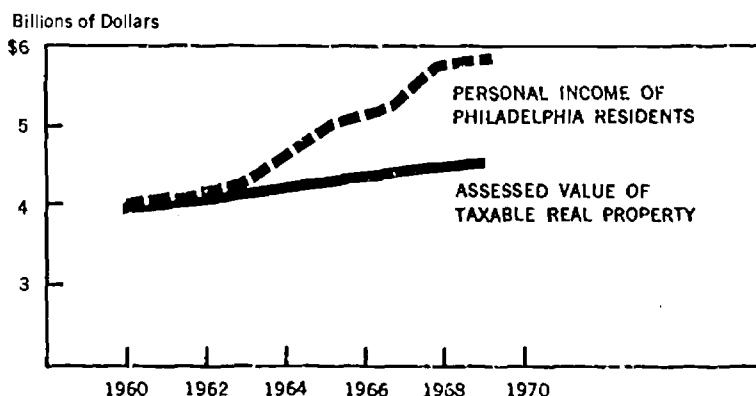


CHART 15  
THE PERSONAL INCOME OF PHILADELPHIA  
RESIDENTS IS CLIMBING FASTER THAN THE  
ASSESSED VALUE OF REAL ESTATE.



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close to those in the nation. (See Chart 15.) The City's wage and earnings taxes—sources of revenue since 1930's—tap the expanding income of Philadelphia residents and non-residents working within the city limits. By emphasizing tax hikes in wages and salaries, City administrators were able to relieve the burden on the sagging real property base. In 1969, real property taxes comprised only 24 per cent of total revenues, compared to 42 per cent in 1952. During the same period, revenues from personal income taxes grew from 30 per cent to 45 per cent of total municipal revenues (Chart 13).

The School District, in contrast, had few alternative taxes to turn to when real property receipts began to lag. Since over 50 per cent of the revenues came from the real estate tax in the early 1960's and the public resisted upping the levy, School District finance administrators turned to the Commonwealth. Active lobbying in Harrisburg for recognition of the crisis facing public education bore fruit. Commonwealth aid for local public education has expanded sharply largely because a new formula for distributing aid reflects some recognition of the higher costs of teaching students in crowded urban centers. From 30 per cent in the early 1960's, Commonwealth aid to the School District of Philadelphia grew to over 50 per cent of total receipts in 1969 (Chart 14).

**A Mixed Blessing.** While intergovernmental aid is a welcome relief, anticipating new levels of aid is often a task full of uncertainty. State governments are facing the same fiscal crunch local governments face, and the task of balancing the books in state capitals is getting tougher each year. Threatened cutbacks, pending legislation, new administrations, and delayed payments—whether at the state or Federal level—all make the job of fiscal management at the local level especially difficult and costly. As the financing of local public services moves fully into the arena of state and national

support during the 1970's, even more difficult budget planning problems may arise.

**The Struggle Continues.** Even with a massive infusion of Commonwealth aid, the School District has had to rely upon the local tax base for new sources of revenue. Hoping to collect \$30 million, the Board of Education began levying a corporate net income tax in 1969. When the returns came in, they found they had missed this mark by nearly one-half—netting only \$15 million. Two new taxes were levied in the 1971 fiscal year: one on the retail sale of liquor and another on commercial occupancy of real estate. But the former was rescinded by the Commonwealth Supreme Court. And current expectations are that the commercial occupancy tax will generate no more than \$15 million in new revenues. As for the City, after hiking the wage tax by 1 per cent in 1969, municipal administrators are now taking a look at the real property tax as a relief from new fiscal headaches.

#### SUMMARY OF PROJECTIONS

Individual projections were made for 21 different revenue sources of the City and School District. Five major sources of revenue have been chosen to summarize our results: Real Property Taxes, Personal Income Taxes, Business Activity Taxes, Non-tax Local Revenue, and Intergovernmental Revenue. With no tax rate increases, total revenue could increase by \$400 million if our medium projection for 1975 holds. Nearly half of this increase (\$170 million) would come from local revenue collections, while the remainder is expected to be new intergovernmental aid. (See Table 15.) New local revenues would give the City \$130 million. The School District would take in \$140 million of the intergovernmental increase.

On the local front, the City's personal income taxes—primarily the wage and earnings taxes—will grow the most heartily. Without rate increases, total personal income tax

**TABLE 15**  
**REVENUES**  
 (millions of current dollars)

	1970	1975 PROJECTIONS		
		HIGH	MEDIUM	LOW
<b>I Real Property Taxes</b>	<b>206.5</b>	<b>235.6</b>	<b>225.0</b>	<b>214.4</b>
City	111.3	127.3	120.7	114.1
School District	95.2	108.3	104.3	100.3
<b>II Personal Income Taxes</b>	<b>209.4</b>	<b>302.4</b>	<b>288.1</b>	<b>274.8</b>
City	201.9	294.8	280.7	267.6
School District	7.5	7.6	7.4	7.2
<b>III Business Activity Taxes</b>	<b>69.6</b>	<b>117.3</b>	<b>111.8</b>	<b>106.7</b>
City	40.8	55.1	52.5	50.1
School District	28.8	62.2	59.3	56.6
<b>IV Local Nontax Revenue</b>	<b>73.1</b>	<b>109.7</b>	<b>107.5</b>	<b>105.3</b>
City	71.0	107.2	105.0	102.8
School District	2.1	2.5	2.5	2.5
<b>V Total Local Revenue</b>	<b>558.5</b>	<b>762.3</b>	<b>730.7</b>	<b>700.5</b>
City	425.0	581.6	557.2	533.9
School District	133.5	180.7	173.5	166.6
<b>VI Intergovernmental Revenue</b>	<b>183.5</b>	<b>484.6</b>	<b>397.9</b>	<b>327.1</b>
City	37.5	128.5	109.9	93.5
School District	146.0	356.1	288.0	233.6
<b>VII Total Revenue</b>	<b>742.1</b>	<b>1246.8</b>	<b>1128.6</b>	<b>1027.6</b>
City	462.5	710.1	667.1	627.4
School District	279.6	536.7	461.5	400.2

receipts would move up \$80 million, according to our medium projection. The School District's business activity taxes—corporate net income, and general business, and the new commercial occupancy tax—will probably show the next strongest growth. At current rates, the School District stands to gain an additional \$30 million by 1975. Equal gains may be registered from the City's nontax revenue sources; however, the bulk of the new collections will be earmarked for debt service.

Overall, our projections for revenue are consistent with the pattern that has emerged since the early 1960's—heavy reliance on the local tax base for municipal services and a healthy support of public education with

Commonwealth aid. The strategies that unfold for meeting rising expenditures in the 1970's will continue to include a delicate balance of tax hikes, new taxes on the local scene, and fiscal support from the Commonwealth and Federal governments.

#### METHODS OF PROJECTION

Most revenues were projected to fiscal 1975 in constant dollars (net of inflation), and then increased in accord with projections of inflation.<sup>4</sup> This method was used in order to take account of the close relation between growth in many parts of the tax

<sup>4</sup> Except for intergovernmental aid and real property receipts which were projected in 1975 dollars.

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base and changes in price levels. Wages, for example, typically increase by a small amount, roughly equal to the gain in productivity, plus whatever change there is in the average price of goods purchased by workers. The relation is not exact. In some years, wages do not go up so much as do general prices, and in other years, they exceed price increases. But over a longer period of time, the efforts of workers to see the benefit of their improved productivity put into wage gains cause wage levels to grow at a rate about equal to the sum of percentage improvements in productivity and expansion in general price levels. Similar kinds of effects are present in other tax bases, with the exception of the base for the real estate tax. In part because the value of the real estate base is determined administratively, and in part because real estate is a form of wealth, it has not tended to be responsive to changes in the general rate of inflation.

Our constant dollar projections of revenues were translated into current dollar (1975) collections using three alternative rates of inflation for the local economy—a high projection of revenues, assuming the price level for consumer products would rise, on the average, 5.5 per cent annually to 1975; a medium projection, assuming a 4.5 per cent rise; and a low projection, assuming a 3.5 per cent average annual increase.

Where possible, we compared tax revenues directly with their tax base. For example, collections from the wage and earnings taxes since 1952 were found to grow at the same rate as did the personal income of Philadelphia residents. Real property tax revenues grew only as fast as taxable assessed value of real estate. In these cases, independent projections were made of the 1975 tax base, from which revenue levels were estimated. Most often, collections—after adjusting for tax rate increases and inflation—showed a slow, regular growth over the years. Where this growth was sufficiently stable, we assumed it would continue

to 1975. Collections in 1975 were projected for tax rates existing in 1970.

Nontax local revenue—the bulk of which accrues to the City—was projected individually for each of several components: municipal licenses, fines, and service charges; rental and debt service payments to the City by public utilities, the Philadelphia port, and International Airport; and miscellaneous revenue going to the School District. In each case, our projection of 1975 collections was founded on past growth of revenues and, where appropriate, on construction plans that may significantly increase rental or debt service receipts.<sup>5</sup>

Intergovernmental aid proved to be the most difficult revenue source to project because its growth has been volatile in recent years and future levels of aid will depend upon the strength of Commonwealth and Federal support. Our medium estimate of total intergovernmental aid to the City assumed recent growth rates will continue. For the School District, on the other hand, we have assumed a slight slowing in the growth rate of subsidies from the Commonwealth. Recent increases have been sizable, but the Commonwealth, itself, faces financial problems. So, continued strengthening of support is uncertain. Consequently, our highest projection—an annual average increase of 20 per cent to 1975—is somewhat lower than the average increase since 1965. A small Federal payment to the School District—used to administer its Federal anti-poverty fund—has been projected to fiscal 1975 on the basis of estimates from School officials.

A detailed summary of the method for projecting each revenue source follows, and in Tables 16 to 20 we present individual projections.

<sup>5</sup> Nearly half of the City's nontax local revenue is earmarked for debt service to pay off revenue bonds. Rental receipts from City-owned facilities like the port, International Airport, and Civic Center are typical examples.

## REAL PROPERTY TAXES

**Real Estate Tax (City and School District).** Collections from this tax were projected as a function of the assessed value of taxable real property in Philadelphia. The assessed value of real property has registered an average annual rate of increase of 1.6 per cent since the late 1950's. In real dollars, this represents a total decline of nearly 3 per cent in the value of the base since 1958. Because a number of factors in addition to the general price level in the local economy determine the level of assessed value (for example, frequency of assessments and amount of tax-exempt property), we projected assessed value of real property in current dollars.

From a level of \$4.6 billion in 1969, according to our medium projection, taxable assessed value of real property in fiscal 1975 will grow to \$5 billion—a continuation of the 1.5 per cent annual rate of growth of the past. High and low estimates were derived from the statistical model used to project assessed value. (See note to Table 16.)

City and School District collections from the real estate tax, adjusted for rate increases, were derived from the high, medium, and low projections of taxable assessed value of real property. Separate projections, assuming 1970 tax rates for the City and School District, are shown in Table 16.

**Real Property Transfer Tax (City).** Revenues from this tax, levied on the sale price of real estate transfers, were projected as a time trend. Collections have been irregular, but small in amount. From a level of \$4 million in 1970, the receipts are projected to reach \$4.3 million in fiscal 1975 (Table 16).

## PERSONAL INCOME TAXES

**Wage and Earnings Taxes (City).** A resident of Philadelphia or a nonresident who works in Philadelphia pays one of these two taxes

on earned income. The wage tax is collected from businesses in the City that withhold the tax from employees' paychecks. Earnings tax collections are from individuals who file separate returns because their employer does not withhold. Many of the payers of the earnings tax are Philadelphia residents working in surrounding counties.

Available data on personal income earned in Philadelphia are incomplete. While both Philadelphia residents and nonresidents who work in the City pay taxes, data on personal income cover Philadelphia residents only.<sup>4</sup> However, actual collections of wage and earnings tax revenues proved to change at much the same rate as did the personal income of Philadelphia residents. Local personal income was projected to fiscal 1975 as a function of U.S. personal income. From this projection, probable revenue collections for 1975 were derived.<sup>5</sup>

Revenues from both the wage and earnings taxes were projected in constant (1968) dollars. As in the case of other revenue projections, an average annual rate of inflation of 5.5 per cent was applied to derive the high revenue projection; 4.5 per cent, for the medium projection; and 3.5 per cent, for the low projection. (See Table 17.)<sup>6</sup>

**Personal Property Tax (City) and Net Income Tax (School District).** The personal property tax of the City is on the value of securities owned by individuals. The School

<sup>4</sup>The Fels Center of Government of the University of Pennsylvania developed a time series on disposable personal income of Philadelphia residents for this study. It is based upon data published by *Sale: Management Magazine*.

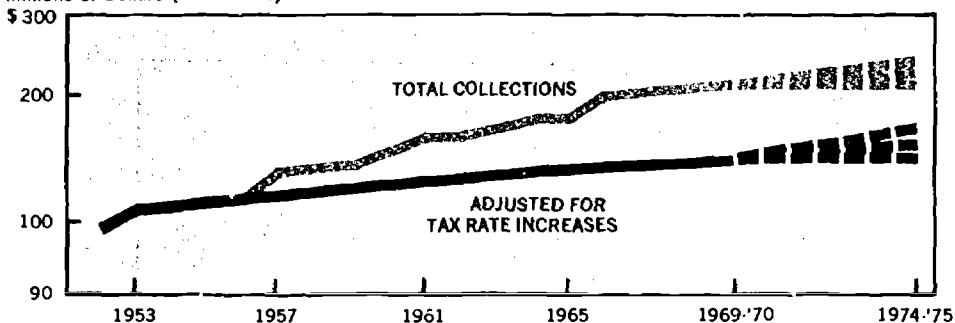
<sup>5</sup>U.S. personal income projections for 1975 were provided by the Economic Forecasting Unit, Wharton School, University of Pennsylvania.

<sup>6</sup>Factors other than inflation may also influence these tax receipts into the 1970's. Most importantly would be a shift in the number of workers commuting into the city. It was assumed that for a five-year period, in-commuters would remain a constant proportion of total employment in the city.

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**CHART 16  
REAL PROPERTY TAX REVENUES**

Millions of Dollars (Ratio Scale)



**TABLE 16  
REAL PROPERTY TAXES  
(millions of current dollars)**

	1970	1975 PROJECTIONS		
		HIGH	MEDIUM	LOW
Real Estate (City) .....	107.2	123.0	116.4	109.8
Real Property Transfer (City) .....	4.2	4.3	4.3	4.3
Real Estate (School District) .....	95.2	108.3	104.3	100.3
Total .....	206.6	235.6	225.0	214.4
City .....	111.3	127.3	120.7	114.1
School District .....	95.2	108.3	104.3	100.3

**METHODS OF PROJECTION**

CITY: Real Estate Tax receipts (rate adjusted) were projected as a function of assessed value\* of taxable real property for the years 1960 to 1969.

Regression statistics:  $r^2 = .98$ ,  $t = 23$ .

The confidence interval of the 1975 estimate at 90 per cent level is \$113 to \$120 million.

CITY: Real Property Transfer Tax receipts were projected as a time trend for the years 1953 to 1969.

Regression statistics:  $r^2 = .49$ ,  $t = 3.7$ .

The confidence interval of the 1975 estimate at 90 per cent level is \$3.5 to \$4.9 million.

SCHOOL DISTRICT: Real Estate Tax receipts (rate adjusted) were projected as a function of the assessed value\* of taxable real property for the years 1960 to 1969.

Regression statistics:  $r^2 = .99$ ,  $t = 29$ .

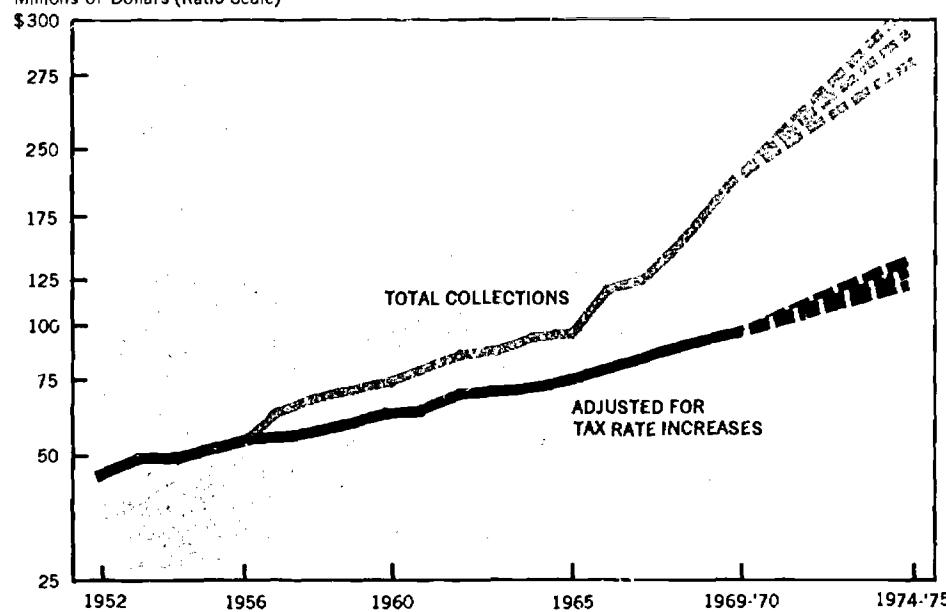
The confidence interval of the 1975 estimate at 90 per cent level is \$102 to \$106 million.

\*Assessed value was projected as a time trend for the years 1952 to 1969.

Regression statistics:  $r^2 = .98$ ,  $t = 27$ .

1975 Projection: \$4,961 million. The confidence interval of this estimate at the 90 per cent level is \$4.8 to \$5.0 billion.

**CHART 17**  
**PERSONAL INCOME TAX REVENUES**  
 Millions of Dollars (Ratio Scale)



District dropped its personal property tax in 1968 and placed a tax on dividends from securities and other income-producing holdings. The change in the tax base of the School District was essentially one from "assets held" to "income from assets."

There has been no real growth in collections from the City's personal property tax since 1960. Our projections for 1975, in constant (1968) dollars, show no increase over fiscal 1970 collections. Inflation could boost receipts to a level of \$7 million. (See Table 17.)

The School District's shift from a tax on the value of personal property to a tax on net income from personal property has had no appreciable impact on revenue collections. As in the case of the personal property

tax of the City, all growth in receipts is likely to come from inflation. (See Table 17.)<sup>1</sup>

**Parimutuel Tax (School District).** This tax was instituted in 1963 with the opening of the Liberty Bell Race Track. Presently, there is a 2 per cent tax on betting for harness and flat racing. Revenues are likely to drop by nearly 50 per cent when flat racing moves from Liberty Bell in 1972. From a level of \$4.4 million in 1970, this tax will garner only \$2.5 million in 1975. (See Table 17.)

<sup>1</sup> Unlike the wage and earnings taxes, both of these income taxes are small producers of revenue, and collection is costly to enforce, given the size of the proceeds.

## FEDERAL RESERVE BANK OF PHILADELPHIA

TABLE 17  
PERSONAL INCOME TAXES  
(million of dollars)

	1970 Actual	1975 PROJECTIONS			
		Constant Dollars	Current Dollars		
			HIGH	MEDIUM	LOW
Wage (City) . . . . .	178.5	183.0	252.0	239.9	228.7
Earnings (City) . . . . .	18.3	25.8	35.5	33.8	32.2
Personal Property (City) . . . . .	5.1	5.4	7.4	7.0	6.7
Net Income (School District) . . . . .	3.0	3.7	5.1	4.9	4.7
Pari-Mutuel (School District) . . . . .	4.4	1.9	2.5	2.5	2.5
Total . . . . .	209.4	219.7	302.4	288.1	274.8
City . . . . .	201.9	214.1	294.8	280.7	267.6
School District . . . . .	7.5	5.6	7.6	7.4	7.2

## METHODS OF PROJECTION

CITY: Wage Tax receipts (rate adjusted) were projected as a function of Philadelphia personal income\* for the years 1954 to 1969.

Regression statistic:  $r^2 = .96$ ,  $t = 19$ .

The confidence interval of the 1975 medium estimate is \$232 to \$248 million.

CITY: Earnings Tax receipts (rate adjusted) were projected as a function of Philadelphia personal income\* for the years 1960 to 1969.

Regression statistics:  $r^2 = .93$ ,  $t = 11$ .

The confidence interval of the 1975 medium estimate is \$32 to \$36 million.

The Personal Property Tax (City) and Net Income Tax (School District) were projected in real dollars as an average of recent collections.

\* Philadelphia personal income was projected as a function of United States personal income for the years 1954 to 1969.

Regression Statistics:  $r^2 = .98$ ,  $t = 25$ .

Medium projection in 1975 dollars is \$8,300 million. The confidence interval of the 1975 estimate at 90 per cent level is \$8,061 to \$8,539 million.

## BUSINESS ACTIVITY TAXES

The four major business taxes levied by the City and School District—Mercantile License Tax, Unincorporated Business Net Profits Tax, General Business Tax, and Corporate Net Income Tax—have shown no real growth since the late 1950's. Inflation and tax rate hikes have accounted for nearly all collection increases. The leveling off of the City's economy in the 1950's and 1960's had its impact on these business tax receipts. We have projected no real increase in business tax collections to fiscal 1975. The high, medium, and low projections shown in Table 18 are based upon inflation in the local economy. The commercial occupancy

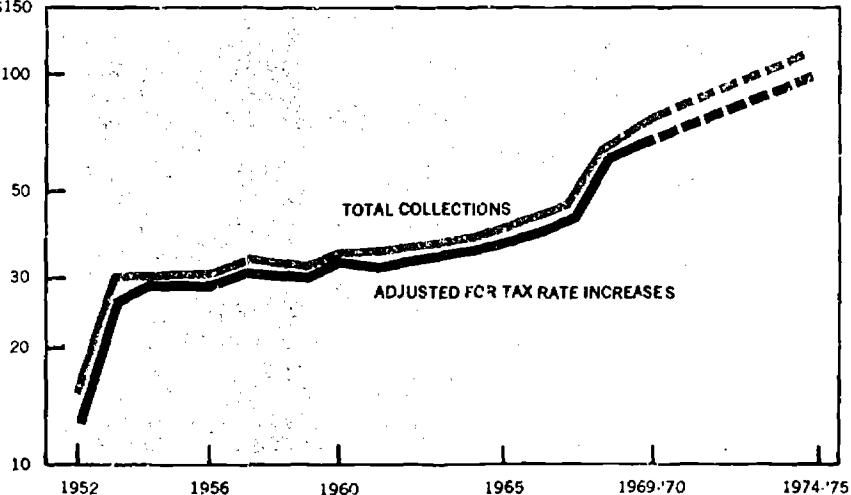
tax, levied by the School District, probably will be the only cause of real increase in business tax collections.

## LOCAL NONTAX REVENUE

**Licenses, Fines, and Service Charges (City).** Collections from more than 150 municipal licenses and permits; charges for health, welfare, and miscellaneous services; contributions; and transfers from other funds comprise this source of revenue. Total collections have shown an irregular growth at an average rate of 4.8 per cent a year since 1960. The base for this revenue source is heterogeneous, so a time trend projection was made for 1975 collections. Assuming no

**CHART 18  
BUSINESS ACTIVITY TAX REVENUES**

Millions of Dollars (Ratio Scale)



significant changes in the rate for service charges, fines, or fees, collections may range between \$32 and \$34 million in 1975. (See Table 19.)

**Utilities (City).** Philadelphia Gas Works (PGW) and the Southeastern Pennsylvania Transportation Authority (SEPTA) pay the City rent and annually make payments on bond issues floated by the City for the utilities. The current rent payment for publicly owned PGW property is \$15.5 million. SEPTA pays \$6.2 million into the City's coffers annually for the leasing of subway and elevated tracks. The City and the utilities periodically renegotiate the rent payments, but both utilities expect to continue rentals

at current levels until 1975.

SEPTA and PGW each use the City as a means to float bond issues and attract buyers. Financing of the South Broad Street Subway will increase SEPTA indebtedness to the City by approximately \$35 million. Principal and interest payments on this amount in 1975 are estimated to be \$3 million. Past City bond issues for PGW plus the recent voter approval of a \$40 million issue will result in \$10.4 million worth of debt service payments by 1975. Our projection of revenues from these two utilities for 1975 is \$35 million. (See Table 19.)

**Debt Service (City).** In addition to receiving payment for debt service from SEPTA and PGW, the City is reimbursed for debt service

## FEDERAL RESERVE BANK OF PHILADELPHIA

**TABLE 18**  
**BUSINESS ACTIVITY TAXES\***  
 (millions of dollars)

	1970 Actual	1975 PROJECTIONS			Current Dollars LOW
		Constant Dollars	HIGH	MEDIUM	
Business Net Profits (City) .....	15.3	16.0	22.0	21.0	20.0
Mercantile License (City) .....	23.4	22.7	31.3	29.8	28.4
Miscellaneous (City) .....	2.0	1.4	1.8	1.8	1.8
<b>General Business</b>					
(School District) .....	12.7	13.4	18.4	17.6	16.9
<b>Corporate Net Income</b>					
(School District) .....	16.1	16.8	23.1	22.0	21.0
<b>Commercial Occupancy</b>					
(School District) .....	0.0	15.0	20.6	19.7	18.7
<b>Total</b> .....	69.6	80.0	117.3	111.8	106.7
City .....	40.8	40.0	55.1	52.5	50.1
School District .....	28.8	40.0	62.2	59.3	56.6

\* See text for assumptions used in projections.

from commuter cars and port facilities. Scheduled payments for these capital investments, including recent bonds floated by the Philadelphia Port Corporation, are likely to reach \$6.8 million by fiscal 1975. (See Table 19.)

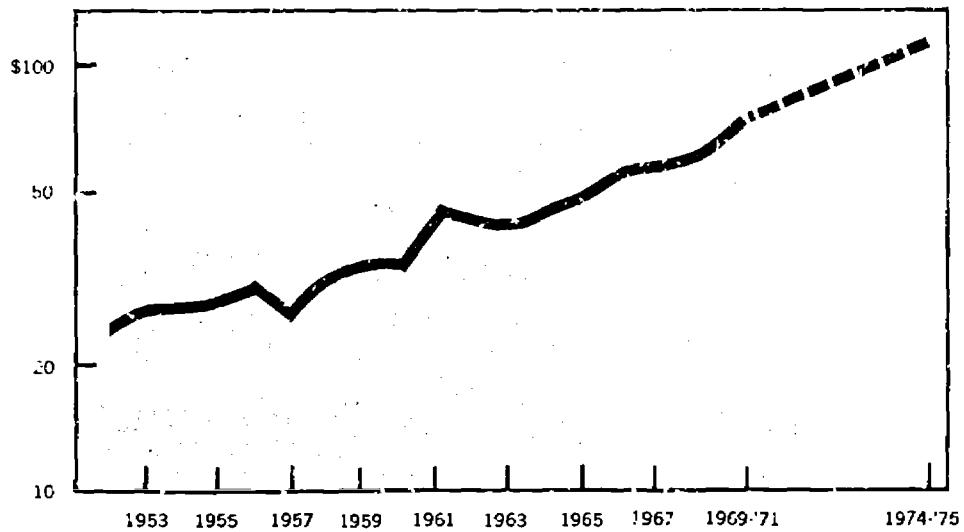
**Civic Center, Port, and Airport Rentals (City).** The convention and exhibition halls in the Civic Center, piers on the waterfront, and International Airport facilities earn rent for the City. Discussions were held with managers of each of these facilities regarding long-range plans for utilizing existing facilities and the construction of new facilities. The most significant change is the expansion in the capacity of International

Airport from 7 to 12 million passengers a year. The City's contribution to Airport expansion—a \$100 million bond issue—was approved by voters in the fall of 1970. Our discussions indicated that rentals from the larger Airport facilities, along with Civic Center and port facilities, probably will reach \$30 million by 1975. (See Table 19.) All revenue so gained will be used to pay debt service on outstanding bonds.

**Miscellaneous (School District).** The School District collects revenues from a number of miscellaneous sources—interest on investments, rental of buildings, special grants, collections in lieu of real estate tax, and many more. According to the School Dis-

**CHART 19**  
**LOCAL NONTAX REVENUES**

Millions of Dollars (Ratio Scale)



trict's official estimate, these revenues will increase only slightly into the 1970's. Our projection is \$2.5 million for fiscal 1975. (See Table 19.)

#### INTERGOVERNMENTAL REVENUE

**City of Philadelphia.** Federal and Commonwealth revenues to the City include both direct grants and reimbursements for services rendered. Payments are scattered among 20 to 30 operating functions, but the bulk of the funds flow to health and welfare programs.<sup>10</sup> Programs which currently receive

a large chunk of intergovernmental aid—maternity and infant care for low-income families, general medical assistance, care and housing of children and the aged, for example—are likely to receive further Commonwealth and Federal assistance in the 1970's. (See discussion on welfare and health expenditures, Appendix.) However, aid to the particular program components is likely to be highly variable. Therefore, intergovernmental aid from both the Commonwealth and Federal government is projected as one revenue source, without designation of program categories.

Three rates of growth for new aid are assumed. A medium projection of a 2.4 per cent average annual rate of growth—somewhat slower than growth since 1965—results in a level of \$110 million in 1975. (See Table

<sup>10</sup> Not included in our projections are intergovernmental grants to the City's Capital Fund. Most of these grants must be matched by contributions from the Capital Budget, which is mainly supported with revenue from the sale of bonds.

## FEDERAL RESERVE BANK OF PHILADELPHIA

TABLE 19  
LOCAL NONTAX REVENUE  
(millions of dollars)

	1970 Actual	Constant Dollars	1975 PROJECTIONS		
			HIGH	MEDIUM	LOW
Licenses, Fines, and Service Charges (City) .....	31.1	23.9	34.0	33.0	32.0
Utilities (City) .....	24.5	26.7	35.1	35.1	35.1
Debt Service (City) .....	2.7	5.2	6.8	6.8	6.8
Airport, Port, Civic Center (City) .....	12.6	23.0	31.3	30.1	28.9
Miscellaneous (School District) .....	2.1	1.9	2.5	2.5	2.5
Total .....	73.1	80.5	109.7	107.5	105.3
City .....	71.0	78.6	107.2	105.0	102.8
School District .....	2.1	1.9	2.5	2.5	2.5

## METHOD OF PROJECTION

CITY: Revenues from Licenses, Fines, and Service Charges were projected as a time trend for the years 1952 to 1969.

Regression Statistics:  $r^2 = .95$ ,  $t=16$ .

The confidence interval of the 1975 estimate at a 90 per cent level is \$30 to \$36 million.

See discussion in text for methods used to project remaining revenues.

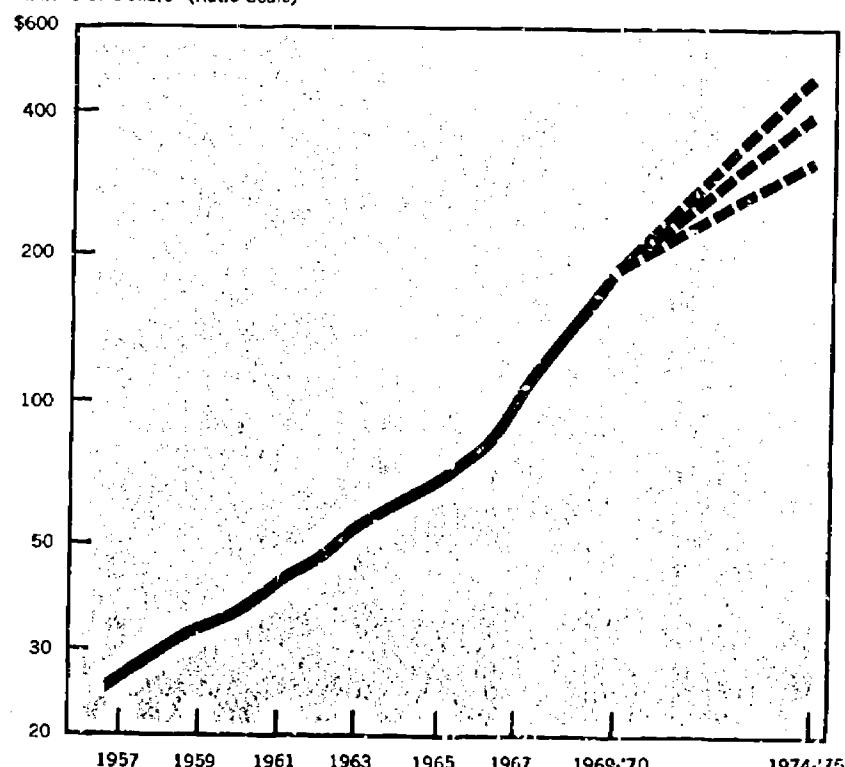
20.) A 20 per cent annual rate of increase will generate \$94 million, our low estimate; and a 28 per cent rate will yield \$129 million, our high estimate. In light of the highly uncertain future regarding new levels of support from Commonwealth and Federal agencies, these projections are likely to be conservative, especially if additional Federal programs materialize in the early 1970's. (See Chart 12 in the article for past levels of intergovernmental aid and our projection.)

**School District of Philadelphia.** Commonwealth support of public education in Philadelphia is crucial to the financial future of the School District. Projecting future rates of growth in aid on the basis of recent history, however, might prove to be overly optimistic. From a base of \$50 million in

1965, Commonwealth subsidies reached \$88 million in 1969, and then jumped to \$140 million in just one year. Including the most recent increment of over \$50 million, the average annual increase has been 28 per cent since 1965.

While public pressure will continue to mount in Harrisburg for special consideration of the higher education costs facing school districts in large cities, the State's coffers may yield somewhat smaller increases than in the recent past. Our highest projection assumes that the yearly rate of growth will slow somewhat from the 28 per cent rate of the 1965-70 period. Assuming a growth rate of 20 per cent annually, State subsidies would reach nearly \$350 million in 1975—a \$210 million increase over 1970 aid (Table 20). Our medium projection—an

**CHART 20**  
**INTERGOVERNMENTAL REVENUE**  
 Millions of Dollars (Ratio Scale)



**TABLE 20**  
**INTERGOVERNMENTAL REVENUES\***  
 (millions of current dollars)

	1970 Actual	1975 PROJECTIONS		
		HIGH	MEDIUM	LOW
City	37.5	128.5	109.9	93.5
School District	146.0	356.1	289.0	233.6
Commonwealth	140.0	348.1	280.0	225.6
Federal	16.0	8.0	8.0	8.0
Total	183.5	484.6	397.9	327.1

\* See text for assumptions used in projections.

FEDERAL RESERVE BANK OF PHILADELPHIA

annual rate of 15 per cent—places subsidies at \$280 million in 1975; with our low projection—10 per cent annually—subsidies would be \$225 million.

As in the case of intergovernmental aid to the City, these projections may prove to be conservative. But, since we have assumed hefty rates of increase, the dimensions of

new aid necessary to fill the projected gap come fully into focus. If the School District were to fill our projected deficit of \$324 million for the 1975 fiscal year entirely with Commonwealth aid, the annual rate of increase in subsidy payments would have to be 27 per cent. (This deficit is shown in article, Table 1.) ■

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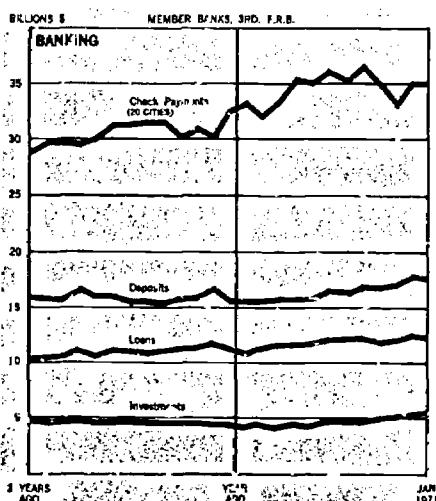
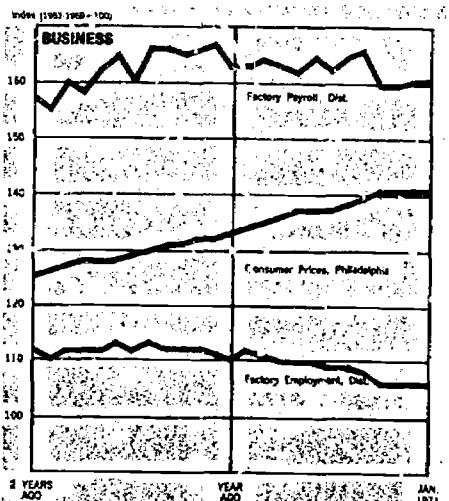
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	Per cent change		Per cent change		Employment		Payrolls		Check Payments**	
	January 1971 from mos. ago		January 1971 from year ago		January 1971 from mos. ago		January 1971 from year ago		January 1971 from mos. ago	
	mo. ago	year ago								
MANUFACTURING										
Production .....					0	- 5				
Electric power consumed .....	- 1	- 2								
Man-hours, total* .....	- 2	- 8								
Employment, total .....	- 1	- 4								
Wage income* .....	- 1	- 1								
CONSTRUCTION** .....	N.A.	- 25	N.A.	- 9						
COAL PRODUCTION .....	+ 6	+ 15			+ 4	+ 16				
BANKING										
(All member banks)										
Deposits .....	- 2	+ 13	- 2	+ 14						
Loans .....	- 2	+ 12	- 3	+ 5						
Investments .....	+ 2	+ 20	1	+ 22						
U.S. Govt. securities .....	- 3	+ 9	0	+ 18						
Other .....	+ 5	+ 27	+ 2	+ 24						
Check payments*** .....	0	4	- 2	+ 12						
PRICES										
Wholesale .....			+ 1	+ 2						
Consumer .....	D\$	+ 78	0	+ 5						

\* Production workers only

\*\* Value of contracts

\*\*\* Adjusted for seasonal variation

†† SMSA's  
Philadelphia

\* Not restricted to corporate limits of cities but covers areas of one or more counties.

\*\* All commercial banks. Adjusted for seasonal variation.

\*\*\* Member banks only. Last Wednesday of the month.